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ABSTRACT

This report sets forth findings of a committee charged with recommending policies to create 10,000,000 new jobs through small business. It defines the problems of American workers and small business owners in a period of dramatic economic change. Emphasis is on solutions for the conditions that nurture enterprise and on what the country needs to do to encourage small business formation, a more secure environment for workers, and economic growth. Findings and conclusions are presented in four major areas: preparing the American people to compete; encouraging greater savings and investing them productively; expanding export groups, including those for small businesses; and minimizing the impediments to the growth of small firms. Five recommendations, outlining institutional mechanisms to focus sustained attention on the problems, are as follows: (1) mobilize the American people, (2) prepare the American work force, (3) invest in the future, (4) restore the "Yankee Trader" tradition, and (5) clear the decks--in other words, institutional reorganization of structures and processes to reflect new realities of global competition. Suggestions for implementation follow each recommendation. Appendixes include annotations--quotations from relevant literature--on numerous current economic concerns. (YLB)

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The National Commission on Jobs and Small Business
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Contents

Preface iv

Members of the National Commission on Jobs and Small Business v

Congressional Conveners vi

Foundation Support vi

Introduction vii

Making America Work Again: Jobs, Small Business, and the International Challenge 1

Findings 15

Recommendations 27

Appendices 45

Preface

Few areas of our national life are as important to our economic health and well-being as small business. Small enterprises represent the economic backbone of communities across the country, the major source of job creation in the United States, and a vital source of the innovation, new products, and services which drive our economy.

These reasons alone were sufficient for each of us to agree to serve as co-chairs of the National Commission on Jobs and Small Business when it was convened in September 1985 by eighteen leaders of the United States Senate and House of Representatives.

Each of us had, in addition, a more personal interest in the success of this significant undertaking. One of us started his career in private life by establishing, in the rural South, a small firm which became an important part of the local economy and earned in its first year exactly $187. The other, as a member of the House of Representatives for many years, represented a midwestern city whose small firms were the foundation of the manufacturing, supply, and distribution systems for the American automobile and furniture industries.

Far from a national abstraction, small business to each of us represents the very heart of economic opportunity in America and a linchpin of our social and economic cohesion.

The Commission has completed its important work, and the conclusions and recommendations in this report deserve the attention of citizens everywhere. Our hope is that the report will help trigger the renaissance of entrepreneurship and business creation needed to carry America successfully into the 21st century.

Jimmy Carter Gerald R. Ford

Jimmy Carter
Plains, Georgia

Gerald R. Ford
Rancho Mirage, California

Members of the National Commission on Jobs and Small Business

Jimmy Carter
Honorary Co-Chairman

Gerald R. Ford
Honorary Co-Chairman

Sam Beard (Chairman)
Wilmington, Delaware
Chairman
National Development Council

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Senior Economist
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Robert Woodward
Atlanta, Georgia
Partner
King & Spalding

James J. Harvey
Executive Director

Congressional Conveners

The Commission was convened on September 10, 1985 by the 18 members of the U.S. Senate and House of Representatives who had urged its establishment. The conveners, representing many of the major committees in the Congress, all regions of the country, and both parties, include:

U.S. Senate

Sen. Lloyd Bentsen
Committee on Finance

Sen. Alfonse M. D'Amato
Committee on Banking, Housing, and Urban Affairs

Sen. Alan J. Dixon
Committee on Small Business

Sen. Slade Gorton
Committee on the Budget

Sen. Sam Nunn
Committee on Small Business

Sen. Warren Rudman
Committee on Appropriations

House of Representatives

Rep. Berkley Bedell
Committee on Small Business

Rep. Lindy Boggs
Committee on Appropriations

Rep. Rodney Chandler
Committee on Science and Technology

Rep. Augustus F. Hawkins
Committee on Education and Labor

Rep. James M. Jeffords
Committee on Education and Labor

Rep. John J. LaFalce
Committee on Banking, Housing, and Urban Affairs

Rep. Trent Lott
Committee on Rules

Rep. Lynn Martin
Committee on the Budget

Rep. Joseph M. McDade
Committee on Small Business

Rep. Parren J. Mitchell
Committee on Small Business

Rep. Henry J. Nowak
Committee on Small Business

Rep. Ed Zschau
High Technology Task Force

Foundation Support

Major support for the Commission was provided by the Charles Stewart Mott Foundation, Flint, Michigan. Other substantial support included:

The Carnegie Corporation of New York (through the Carnegie Forum on Education and the Economy)

The John D. and Catherine T. MacArthur Foundation, Chicago, Illinois

The Andrew W. Mellon Foundation, New York, New York

The National Development Council, New York, New York

The Rockefeller Foundation, New York, New York

Introduction

In September 1985, a bipartisan coalition of members of the House of Representatives and the Senate of the United States established the National Commission on Jobs and Small Business and charged it with recommending policies to create 10,000,000 new jobs through small business.

It has been my privilege to chair this endeavor, and, on behalf of the members of the Commission, it is my pleasure to transmit this report, ***Making America Work Again: Jobs, Small Business, and the International Challenge***, to the 100th Congress of the United States.

Our job creation goal required us to define the problems of American workers and small business owners in a period of dramatic economic change. The candid and vigorous deliberations of the Commission concentrated the search for solutions on the conditions which nurture enterprise and, in that context, on what the country needs to do to encourage small business formation, a more secure environment for workers, and economic growth.

When the Commission first met, President Reagan spoke of the invaluable economic contributions of the small business owner when he said, "Free enterprise and entrepreneurship are the roots of a healthy economy." This report builds on that insight.

In going about its work, the Commission relied on several sources of information: papers commissioned from experts on a variety of business, economic, and education issues; surveys of small business owners and corporate chief executive officers; eight intensive hearings around the country on a

variety of issues affecting small firms; existing analyses of problems in American business from several public and private sources; and the debates, papers, and resolutions prepared for the 1986 White House Conference on Small Business.

During 15 months of study and investigation, the Commission heard from the leaders of the small business community, from delegates to the White House Conference, from members of Congress and the executive branch, from state and local officials, from executives, academic, financial, and corporate leaders, and from the people whom small businesses employ.

We heard from several of the owners of America's 15 million small firms. By nearly any measure they represent a formidable economic force. They employ nearly half of the private non-farm workforce in America, and produce 47 percent of the country's gross domestic product.

We were impressed with the diversity of their opinions as well as with the sense of optimism which characterizes their attitude toward American business life. The members of the Commission mirror that diversity and optimism for the future despite our concern with the enormous economic changes that threaten our people's standard of living unless the country attends to them now.

A complete list of all those who helped make this undertaking possible is included in the appendices which complete this volume. We are, in particular, grateful to those witnesses who took the time, often at their own expense, to provide us with the benefit of their experience. In all cases, the Commission has taken their views into account even if the conclusions in this report differ from their suggestions.

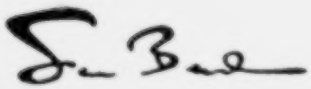
A special word of appreciation is due the four Congressional leaders who planned the announcement of the Commission's establishment—Senators Sam Nunn (Georgia) and Slade Gorton (Washington) and Representatives Parren J. Mitchell (Maryland) and Lynn Martin (Illinois). Without their assistance, our efforts would have been considerably more difficult.

I must also express my admiration for the members of the Commission. Each devoted long hours and days, without

compensation, to this work. As a group, the Commissioners brought to this undertaking not only their energy and the experience of their diverse backgrounds, but also a commitment to the public interest, to small business, and to our goal of creating ten million jobs. Their skill, intelligence, and good humor throughout our investigation made it succeed; their willingness to accommodate the diversity of opinion on the Commission made this report possible. Each Commissioner would probably have written a somewhat different report, but all were in agreement with the central messages of *Making America Work Again*.

The Commissioners join me in thanking the members of the staff for their energetic organization of our activities. Particular thanks are due to James J. Harvey, executive director of the Commission, for his contributions to our work and for his assistance in drafting this report.

Finally, the Commission acknowledges the debt it owes to William S. White, president of the Charles Stewart Mott Foundation, Flint, Michigan. His vision of the need for the Commission sustained us in the months of planning, and his support during our tenure made this report possible.



Sam Beard
Chairman

The American people need to be clear about the significance of the American promise. It represents far more than a platitude. At the core of the promise is our national affirmation of the dignity of the individual. The pledge that all can create their own destinies holds a powerful appeal to people around the world and is . . . the foundation of our national economic growth. That promise animates and sustains small business.

Now the legacy is itself imperiled.

It is time America came to its senses. Wishful thinking and dated views about our place in the world have obscured the domestic effects of international economic competition. Because each generation of Americans has exceeded the standards of its parents in health, income, education, and material well-being, we have long taken our prosperity for granted. But now, a new prospect emerges: for the first time in recent history, our children's standard of living may not equal, much less exceed, our own.

The outlook for the next generation is troubling. Our country is unable to sell many of its products at competitive prices on world markets. Too many of our people are unemployed or underemployed. Several of our great industries are in trouble. Even our advantages in technology and agriculture are fading rapidly. Our ability to meet our obligations as a world leader is threatened by the erosion of the nation's competitive position in commerce, industry, and technology.

Our society seems to have forgotten one of the important truths on which it was founded: in a democracy it is not the government that creates wealth, but the people and their belief in themselves. Adrift from that mooring, we have lost

sight of the commitment and hard work critical to maintaining our international standing. We have forgotten also that just as individual rights are the foundation of political liberty, individual enterprise is the foundation of national prosperity.

The times test us. A secure future for our people means responding to the challenge before us with the energy, dedication, and creativity that characterize American business and labor at their best. In this effort, the values of the entrepreneur and the industry of our workforce are genuine assets in the search for change and renewal.

The Commission's mandate reflected the desire of Congress to reduce unemployment by creating ten million jobs through small business. This report addresses the health of the economy as a whole as well as the health of American small business. The Commission was convinced that the problems of small firms are best understood in the context of the national and international economic forces that exert such a powerful influence on American employment and unemployment. By presenting a realistic assessment of where we stand, this report offers the country the opportunity to rethink the potential of entrepreneurs and small business as a force for economic growth.

Sustaining the creativity and growth of small business is crucial to our national vigor. Small firms employ half of our private workforce and produce half of our gross domestic product.

This Commission does not pretend that small business alone can bear the burden of restoring the competitiveness of the United States. We maintain, however, that the initiative and flexibility of small firms can play a vital role in the vigorous, growing economy essential to securing America's place in the world. And we insist that sustaining the creativity and growth of small business is crucial to our national vigor. Small firms employ half of our private workforce and produce half of our gross domestic product. They created nearly two thirds of the new jobs of the last decade and were one of the driving forces behind our advances in technology. Small business represents a powerful resource.

Against a backdrop of relentless change, one domestic imperative stands out: during the next five years, virtually every community in America will have to replace 50 percent of its jobs and businesses. The question is: where will our people find employment?

Although the developments we describe are cause for concern, they are not occasion for alarm. The jobs will be

The Small Business Dimension

According to the Internal Revenue Service, there were over 15 million small firms in 1983, including ten million sole proprietorships, 1.5 million partnerships, and three million corporations. The Small Business Administration (SBA) estimates that about five million of these businesses are actually full-time enterprises with employees.

There is no generally accepted definition of a "small business." Most analysts rely on the number of employees, but there is little agreement on how many. MIT analyst David Birch, the pioneer in small business job generation research, concentrated on firms employing 100 or fewer workers, and attributed most new jobs to a subset of these firms—very small firms employing 20 or fewer people. Others believe 200 is an acceptable limit; the SBA decribes some industries as "dominated" by small business, defined as firms employing 500 or fewer workers.

Small firms provide a remarkable array of products and services. They forge tools and dies, build houses, design and build sophisticated electronic equipment, repair automobiles, manufacture wiring assemblies, mine the earth, program computers, and produce new medical procedures and breakthroughs. The list is nearly endless. They are major employers in mining, manufacturing, transportation, communications, finance, insurance, and real estate. According to SBA data, small firms dominate employment and sales in wholesale and retail trade, agricultural services, forestry, and construction.

Among the contributions of small business to the overall economy:

- **Employment.** Firms with fewer than 100 employees account for 34 percent of all private, non-farm employment; those with 500 or less employ 48 percent of that workforce. Professor David Birch of the Massachusetts Institute of Technology reported six years ago that "60 percent of all new jobs in the U.S. are generated by firms with 20 or fewer employees," an analysis confirmed by studies of local job generation on Long Island, and in Wisconsin, Massachusetts, and California.

- **Gross National Product.** According to the Small Business Administration, small firms produce 38 percent of our GNP and 47 percent of our gross domestic product, that part of the GNP generated by private firms using resources in the United States.
- **Training.** Small firms give two out of three American workers their first jobs, thus making a significant contribution to the education and training of our workforce.
- **Innovation.** In 1986, the Department of Commerce estimated that small companies generated about "50 percent of all major innovations in the past 30 years." A recent study of 635 successful product innovations in the 1970s attributed 40 percent of them to small business and indicated that small firms brought these innovations to the market much faster than larger firms.
- **Opportunity.** Data from the SBA and the National Federation of Independent Business indicate that the number of women-owned businesses has been increasing three times as fast as that of businesses owned by men, and that the number of self-employed blacks and Hispanics has increased substantially in the last ten years.

there—if we prepare ourselves now. The Commission advances a fundamental proposition that has guided us in our work: global competition is the basic economic reality of our time. It has exposed the shortcomings of our educational

The jobs will be there—if we prepare ourselves now.

system. It has laid bare the lack of corporate readiness to compete. It has forced us, in the most recent recession, to rely on small business as the only source of additional jobs in the United States. And it has underscored the necessity to make competitiveness the touchstone of America's economic policy as we make ready to live in a new age and a different world.

A Different World . . .

The world of 1987 is far different from that of 1950. A generation ago, a triumphant United States lay secure in its borders, confident of its destiny, and pre-eminent in manufacturing and commerce. We had many advantages others did not: a skilled workforce, productive industries, and a rich and bountiful land. The goodwill of the United States financed the recovery of the free world, and our arms shielded friend and former foe alike as they rebuilt their industrial capacity.

The era of American advantage is over. Modern management and finance, technology, and the worldwide increase in the education and skills of workers have created a global economy. This new international economy has raised standards of living around the world and opened our vast domestic markets to determined competitors. Today, products can be designed in one country, engineered in another, produced in yet a third, and distributed around the globe. Shrewd intelligence, diligently applied, explains why watches once assembled in Switzerland, motorcycles built in England, lenses ground in Germany, and automobiles, steel, and television sets made in America are now manufactured around the Pacific Rim.

. . . And Its Consequences

Lacking a strategic response, we have watched our great manufacturing enterprises falter and our industrial

workforce suffer the worst employment shocks in 50 years. We are unable to provide productive work for large numbers of our citizens; we are unwilling to invest adequately in the plant, equipment, education, and technology essential to our international competitiveness; and we borrow more than we are willing to save, preferring to finance consumption at home by piling up debts abroad.

The Commission cannot overstate the seriousness of the economic difficulties now facing the United States. Unchecked, they promise grave consequences for the future.

We borrow more than we are willing to save, preferring to finance consumption at home by piling up debts abroad.

- **A Debtor Nation.** In 1985, for the first time in 75 years, the United States became a debtor to the rest of the world; a year later, the U.S. had become the largest debtor nation in history.

- **Exports.** The American percentage of world exports, measured in constant dollars, shrank by nearly one third between 1960 and 1984. Even in such high-technology industries as aircraft, computers, engines and turbines, scientific instruments, and semiconductors, we have lost world market shares. In 1986, American agricultural trade accounts were in deficit for three months in a row—the first such deficits in 27 years.

- **Productivity.** Since 1970, the growth of American productivity has been cut in half.

- **Growth of the Deficit.** According to the Office of Management and Budget, the national debt doubled between 1980 and 1985. Large annual federal deficits accelerate the growth of the debt. The debt increased at an annual rate of 2.8 percent from 1954 to 1975, at a rate of 11.9 percent from 1975 to 1980, and at a rate of 16.1 percent from 1980 to 1985. Interest on the debt in 1985 totaled nearly $180 billion.

- **Income.** Real wages and salaries, the income on which most families depend, have been falling since 1972. The decline has been virtually indiscriminate: workers in construction, services, finance, insurance, real estate, and manufacturing have all felt the effect. Real personal income per household—including rents, dividends, and interest—shows a similar pattern.

- **Loss of High-Wage Jobs.** We are losing jobs paying $25,000 and more a year in both large and small manufacturing firms and replacing them with jobs in services and retailing paying less than half that amount. Since 1980, America has suffered a net loss of over one million production jobs in manufacturing, paying an average of $13 an hour. At the same time, jobs in services and retail trades, paying between $5 and $7, have increased by 5.5 million.

- **Unemployment.** Unemployment has risen by nearly two percent in each of the last three decades— averaging 4.8 percent in the 1960s, 6.2 percent in the 1970s, and 8.1 percent between 1980 and 1985.

America, meanwhile, has become an import sponge.

- **Automobiles.** By next year, Japan will be the third largest U.S. automaker. By 1990, foreign automobiles, made here and abroad, will account for more than 40 percent of domestic sales.

- **Consumer Electronics.** The market for other consumer goods, particularly in electronics, tells a similar story: we no longer manufacture black and white television sets, and 50 percent of our color televisions and two thirds of our radios come from abroad.

We no longer manufacture black and white television sets. . . . Seventy percent of American manufactured products are subject to foreign competition in the United States.

- **Manufactured Products.** Seventy percent of American manufactured products are subject to foreign competition in the United States, often with subsidies from their own governments more than four times the assistance available to American exporters.

- **Steel and Textiles.** Since 1960, American steel and textile industries have been badly battered. Imports now account for more than one quarter of the steel used in this country, and since 1970 the U.S. share of world crude steel output has declined from 20 percent to 11.6 percent. The textile trade deficit rose by 16 percent in 1985 and textile employment continued its decline.

These developments help explain why the United States, which between 1891 and 1971 never showed a deficit in its international trade account, has recorded a trade deficit nearly every year since 1971. Trade deficits in the 1980s have grown at an alarming rate. The deficit in 1980 stood at slightly under $30 billion; in 1986, it approached $170 billion.

This array of factors also explains why this generation's concern for the material well-being of its children is well placed. We can already see the signs of these pressures squeezing the American middle class. Too large a proportion of our people live in poverty, and recent economic improvements appear to have benefited those of greatest wealth.

The human consequences of these developments cannot be dismissed. Allowing foreign producers to win domestic markets has helped displace 1.1 million production workers since 1980. Predictions of a brighter outlook for urban America have not borne fruit for the unemployed young men and women of our cities. One witness warned the Commission, "Today we are raising a whole generation that feels it has nothing to lose because it has never experienced even the remote hope of being able to find a job. More than 40 percent of black teenagers are jobless." The 100,000 small farmers who went bankrupt last year find scant comfort in knowing that their farms were swept away because over-extended credit could not cope with fluctuating markets.

Comparable threats to our prosperity and security once evoked a unified and vigorous response from the country. American brains and brawn rose to the challenges of the Industrial Revolution in the nineteenth century and the launching of Sputnik in the twentieth. But we search our

The powerful dynamics of the global economy and technological innovation dictate that communities across the country must replace their existing jobs with new ones as the world around them changes.

recent history in vain for a similar response to help us compete in the dynamic global economy.

Despite encouraging demographic trends indicating that the economy will not need to absorb as many young people, creating jobs remains a pressing national need. That need is grounded in a new calculus: the still more powerful dynamics of the global economy and technological innovation dictate that communities across the country must replace their existing jobs with new ones as the world around them changes.

Our economy is not developing apace. Our industry and our government have not responded to the challenge before us by making competitiveness the linchpin of our economic policy. In consequence, we have failed to make the investment in plant, equipment, and machinery necessary to improve our productivity. We have too long ignored the levels of education, training, and skill required in the new workforce. Nor have we capitalized on many unique advantages, including the remarkable ability of the small business community to innovate, to respond to change, and to create wealth and employment.

Threat and Promise

It is easy to lose sight of what is at stake. We are distracted on all sides by strong, determined competitors and by the constant change in the demand for goods and services. We take comfort in material success without understanding that the recent growth of the nation's debt is supported with foreign capital, that too many companies are bowing to the pressure for quarterly profits at the expense of long-term growth, and that, increasingly, two wage-earners are needed to maintain today's family.

We are witnessing nothing less than a fundamental threat to the promise first made in America—that all persons, no matter their station in life, could go as far as the reach of their talents, ambition, and hard work. Although we have not always honored that promise equally for all of our citizens, it has spread the blessings of liberty and prosperity more widely in the United States than in any society known to human history.

The American people need to be clear about the significance of the American promise. It represents far more than a platitude. At the core of the promise is our national affirmation of the dignity of the individual. The pledge that all can create their own destinies holds a powerful appeal to people around the world, and explains why generations of foreigners have sought a better future for themselves and their children on these shores. In offering all citizens the opportunity to pursue their hopes and dreams, the American dream is the source of social mobility in the United States and the foundation of our national economic growth. That promise animates and sustains small business.

Now the legacy is itself imperiled. At stake is not only a fundamental characteristic of the American tradition, but also an element indispensable to the restoration of our economic health and material well-being: the conviction that the individual aspirations of workers, entrepreneurs, and small business owners are a powerful economic force.

It is easy to gloss over one of our hidden strengths. Part of the genius of the American experiment lay in the proposition

that political freedom is essential to economic growth. Innovation, the engine of the modern world, prospers only in an environment that encourages new ideas, even at the expense of the old. Our generation's debt to those who 200 years ago created this republic extends beyond gratitude for their foresight in securing democratic government. In fusing liberty and enterprise, they created democratic capitalism, a system of values unparalleled in its potential for creating and broadening wealth.

Now, as we enter our third century, our task is to fulfill the promise of democratic capitalism by encouraging every citizen to participate productively and competitively in the new world economy.

Small Business and the American Future

The Commission believes that the country has at hand the strategic resources needed to realize that promise:

- **Working Spirit.** The spirit of American working men and women who made this nation the most productive enterprise in the world, and who are eager, once again, to make the proud boast "Made in America" the mark of excellence.
- **Business Skills.** The skills of business owners and entrepreneurs in developing new products and services, and their adroitness at identifying and serving new markets.
- **Intellectual Resources.** The great intellectual and technical resources available in our schools, colleges, universities, laboratories, and workshops. They nurture imagination, the soul of technology.
- **Wealth.** A concentration of wealth and financial resources unmatched elsewhere, combined with the most sophisticated capital markets in the world.
- **Technology.** The unrivaled potential of technology, properly applied, to multiply the productivity of labor and capital, reduce costs, improve reliability, and enhance the quality of working life.
- **Confidence.** The confidence of Americans which makes all of us—employer and employee alike—eager to compete as long as the rules of the game are clear, the playing field level, and the referee impartial. That distinctive American trait has emboldened pioneers, immigrants, and entrepreneurs to stake their futures on their dreams.

Urgently needed is the leadership to fashion a national response from these resources to reinforce the bond between private gain and public good. The recommendations in this report present a framework for such a response and, we believe, a compelling agenda for the leaders of American business, government, and public opinion. But the motivating force behind that consensus comes from yet another, more powerful source: the spirit of enterprise itself.

The Spirit of Enterprise

The spirit of enterprise is essential to the dynamic of the American economy. It explains why impoverished students struggle for an education. It fuels the "intrapreneurial" activities of large corporations, intent on generating new ideas and products. It often motivates the nation's foundations and universities in their dedication to defining and solving problems. Properly nurtured, the spirit of enterprise can give life and direction to the many efforts, public and private, required to rebuild our economy.

At its best, small business typifies that spirit. Business incorporations have increased at a phenomenal rate in the United States in the last generation—from less than 100,000 annually in the 1950s to nearly 700,000 in 1986. Although indicative of the direction of change, these numbers are imprecise. No accurate measure of new business formation,

Properly nurtured, the spirit of enterprise can give life and direction to the many efforts required to rebuild our economy.

including data on self-employment and firms with employees, exists. Incorporation, in fact, may indicate nothing more than the intention to start a firm. Nevertheless, the trend is clear: entrepreneurs have spawned new businesses, indeed whole industries, while mature firms have struggled with changes in the business environment.

Small firms employing 500 or fewer workers account for nearly 50 percent of private employment and half of our gross domestic product. In the aggregate, those small firms employing 100 people or fewer provide jobs for as many workers as large firms employing 500 or more. According to the President's 1986 report, *The State of Small Business*, employment in industries dominated by small firms grew by more than five percent in 1985. By contrast, employment in

industries dominated by large firms grew by less than one percent. The difference continues a pattern of small business job generation stretching back to at least 1976. Studies of job generation over the past ten years show that when job gains and losses for both large and small firms are tallied, small businesses are responsible for more than 60 percent of the new jobs. During the 1981-82 recession, small businesses generated twice the number of new jobs that large businesses lost, in effect accounting for a net gain of one million jobs.

The vitality of American small business lies also in its ability to diversify economic opportunity.

Numerous studies demonstrate the record of invention and innovation of American small businesses. Their contributions are not simply to job generation but also to the training of America's workers, two thirds of whom take their first jobs with small firms.

Other analyses document the fundamental importance of small firms to our national economic strength. In many ways they act as the yeast in our economy, helping to sustain the entire structure. Inter-industry relationships are pervasive and subtle: analyses by the Congressional Research Service indicate that the 1981-82 recession in the housing industry, which is dominated by small businesses, depressed steel and copper orders in the United States as much as did the decline in the automobile industry. The Commission's surveys demonstrate that three quarters of America's great corporations rely on small firms as suppliers, manufacturers, distributors, and customers; four out of ten large firms deal with 1,000 or more small businesses each year. In fact, every automobile worker in manufacturing is supported by four other workers who provide supplies, sales, and services.

This spirit of achievement stands in marked contrast to the flagging economic energy of much of Europe.

The vitality of American small business lies also in its ability to diversify economic opportunity. In the last ten years the number of businesses owned by women has increased three times as fast as that of businesses owned by men. Minority-owned businesses have also grown: the number of self-employed blacks has risen by nearly 50 percent in the last

decade, and the number of Hispanic-owned businesses now stands at over 400,000.

It is evidence of the optimism and skill of our business men and women that this spirit of achievement has persevered in even the most difficult economic times. It stands in marked contrast to the flagging economic energy of much of Europe. The accomplishments of small business can no longer be taken for granted as we chart the course of our economic future.

A Simple Prescription

Building on these accomplishments, we can breathe new life into the American economy. A clear and simple prescription can serve as the nation's guide: attend to the conditions that encourage entrepreneurship, business formation, and job creation, or continue to lose ground to others who do.

This precept has served our nation brilliantly in the past. The great industrial and commercial concerns of our nation were built by innovators such as Ford and Bell whose small businesses grew to help shape a new American economy. Our task is to foster the conditions in which their successors can flourish in the new world around us.

Attending to the conditions of entrepreneurship is not a vague national abstraction. Nor are the consequences remote from everyday life. The imperative we espouse touches every town, home, and life. As David Birch of MIT told the Commission, each year we lose nearly ten percent of our jobs and our businesses large and small. Just to break even, he said, every locality in America must replace half of its jobs every five years. Some areas face an even more formidable task: Texas officials told the Commission that simply to stay abreast of change and population growth, they need to create two million jobs within the state by the year 2000.

The best hope of these communities lies in emulating those localities which have already replaced jobs in ailing industries with jobs created by the spirit of enterprise. For example, 10,000 jobs lost in Birmingham, Alabama's steel mills between 1975 and 1985 were replaced by more than 60,000 new jobs in services, many of them in medicine, medical research, and related technologies. Ten years ago the unemployment rate in Massachusetts was the highest in the country as its textile and leather goods industries went under. Today the state's unemployment rate is among the nation's lowest. The state's schools and universities were the base from which entrepreneurs, starting company after company, replaced every one of the 225,000 jobs swept away a decade ago. Most of these new jobs offered outstanding wages, salaries, and working conditions in an effort to attract the highly skilled workers required in new, technologically innovative firms.

Attending to the conditions of business formation promises a growing economy that can employ our people, support our standard of living, and again make American products and services competitive in world markets. Several conditions require priority attention:

Above all, we must bend every effort to give the challenge of international competitiveness pride of place on the nation's economic agenda. . . .

- Above all, we must bend every effort to give the challenge of international competitiveness pride of place on the nation's economic agenda and in our people's thinking. We must understand, not only intellectually but also as a matter of national practice, that our economy is not self-contained, that the marketplace of America is the world, and that our future lies in developing — now — the ability to compete there vigorously.
- The productivity of our workforce and the inventiveness of our scientists and engineers must be multiplied through education, training, and increased support for research, development, and technology transfer.
- The savings of our people must become more disciplined and more oriented toward improving productivity; new private mechanisms to encourage investment in smaller, growing firms must be developed.
- Finally, the public policies, and private organizations and mechanisms of the American economy that support the competitiveness of our small businesses must be strengthened where they exist and created where they do not.

These conditions hold out a vision for a vital America, renewing the promise of the dignity of productive work — if our people are prepared. This vision promises a sound economy, capable of advancing our nation's goals — if our people are productive. A prosperous economy promises new opportunity for our workers, entrepreneurs, and small business owners — if they can but seize it.

Findings and Conclusions

This section presents the findings and conclusions of the Commission in four major areas: (1) preparing our people to compete; (2) encouraging greater savings and investing them productively; (3) expanding export opportunities, including those for small businesses; and (4) minimizing the impediments to the growth of small firms.

Much of what we have to report causes us concern, not only because of the impact of these factors on businesses large and small, but also because of the complexity of the environment in which these difficulties are embedded. Demographics, tax policy, and the productivity of workers abroad affect our workforce nearly as much as the foresight of our leaders in government, business, and industry. Although these broader issues frame our thinking, our task is not so much to analyze causes as to address consequences. Our findings and conclusions, therefore, are the basis for recommendations on what needs to be done, not a brief for assigning blame.

Our People Unprepared

Of particular concern to the Commission are signs that our people are not armed with the knowledge they need to deal with the changes around them. Two weaknesses stand out. First, the quality of our workforce—blue- and white-collar alike—must be improved. We must act on our understanding that education bears directly on our economic health and well-being. Second, that educational effort must be more firmly grounded in a clear perception of the changed conditions of enterprise in the modern world and of the dynamics of the economy that supports us.

We must act on our understanding that education bears directly on our economic health and well-being.

Education and the World of Work

The speed of change in today's business world demands unprecedented levels of skill, commitment, and flexibility on the part of our workers and managers. Our educational institutions are not, in the Commission's view, preparing our young people for the lifetime of change that lies before them.

Too many young people, even the well educated and well trained, are unable to bring the skills they have acquired to the tasks before them in productive and competent ways. Nor has our workforce acquired the ability to reconfigure those skills to meet new challenges and solve new problems. Even our schools of business have concentrated on developing executives to manage people, wealth, and resources, largely ignoring the need to develop the entrepreneurial talent to create wealth and resources.

Too often a weak educational program in our schools and colleges is followed by an inadequate system for delivering continuing education and retraining to the workforce. Many students appear content to do the minimum necessary to obtain their secondary certificates or college diplomas, hoping to slide by in their adult years with what they learned in the first 20. And, while other countries consciously work to train and retrain large portions of their workforces each year, we seem content with uneven efforts to provide training and retraining for only one half of one percent of ours.

There is widespread agreement that serious attention must be paid to upgrading the skills of the American workforce:

- **Functional Illiteracy.** Millions of Americans are, for all intents and purposes, illiterate, unable to comprehend the simplest written instructions. Although precise figures on the number of illiterate Americans are a matter of debate, the economic impact of widespread illiteracy is beyond dispute. Figures from the 1980 Census indicate that about 75 percent of the unemployed are "functionally illiterate," and the Business Council for Effective Literacy estimates that welfare and unemployment support related to illiteracy costs up to $6 billion annually.
- **Skills of Secondary School Graduates.** The reports of many recent commissions and other prestigious bodies

concerned with education have documented the declining skill levels of the average high school graduate. Of particular concern to this Commission are the findings of the National Assessment of Educational Progress (NAEP) indicating that "higher order" skills such as reasoning, problem solving, and writing are substantially below the standards required for success in the modern world. For example, in a 1986 NAEP examination of writing skills, only 25 percent of 11th graders were judged "adequate," raising serious questions about their ability to succeed in school, business, the professions, or government.

- **No Coherent Training Policy.** Vocational schools, community colleges, public service employment, and youth training activities strive to train and retrain the workforce, but there is no sustained, coherent public policy toward training to support them. Since 1962, the federal government has adopted and abandoned 14 different training strategies. Greater stability in these efforts would surely produce better results.

- **Engineering Shortage.** Half of the students in American graduate schools of engineering are from foreign countries. Our supply of highly skilled engineers, and the teachers who will one day train them, is seriously threatened. Not only are we failing to educate the new generation that will develop and implement our own manufacturing technologies, we are exporting the trained talent that strengthens our competitors in world markets.

By the year 2000, America may have a shortage of as many as 15 million scientists, engineers, skilled mechanics and semi-skilled workers.

We can do better. Indeed, we have no choice: analyses by Nobel Laureate Wassily Leontief, professor of economics at New York University, indicate that the rate of technological change in American work life portends a deepening crisis in the skill levels of our workforce. By the year 2000, America may have a shortage of as many as 15 million scientists, engineers, skilled mechanics such as machinists, and semi-skilled workers including assemblers and welders. A similar number of managers, sales personnel, and clerical help will face a glutted job market and unemployment.

Understanding the Changed Conditions of Enterprise

Several analysts and surveys point to a widespread lack of understanding of our economic difficulties and of the workings of our economy:

Even as foreign competition stalks domestic markets, only a fraction of our businesses export their products.

- **New Competitive Environment.** There are several indicators that neither our businesses nor our leadership are reacting appropriately to new international conditions. Even as foreign competition stalks domestic markets, only a fraction of our businesses export their products. The rapidly changing economy poses a fundamental challenge to the traditional view of work and career: all of us can expect multiple job and career changes during our working lives. Our diplomatic and commercial interests are tongue-tied by the inability of Americans to speak the languages of other lands or to understand their cultures.
- **No Understanding of Entrepreneurship.** University of Michigan researcher John Jackson testified before the Commission that the public has little or no understanding of the job-creating role of small business in the United States, or of the contributions of entrepreneurs.
- **Lack of Knowledge of Economics.** A disquieting number of American high school students, according to the Joint Council on Economic Education, do not understand how the American economy works. Surveys indicate that education in economics is not required for high school graduation in most states and school districts. In consequence, students are unfamiliar with the role of business, government, and labor in the economy; nor do they grasp such basics as supply and demand, the importance of trade, and the relationship between productivity and wages.
- **Educators Equally Uninformed.** Educators are equally uninformed. Far from understanding capitalism as a system for creating wealth, many of them think first of its excesses. Few American schoolteachers have completed even a single economics course in college, and only eight percent of American adults were taught economics in school. Nearly seven times as many adults report that their understanding of economic issues comes mainly from commercial television.

Surely it is not too much to ask that our schools provide graduates with the knowledge of the changing conditions of the world in which they must earn a living. Despite isolated efforts, most students appear to leave school underinformed—even misinformed—about economic matters, including the role of business in American life.

Savings and Investment Inadequate

At the heart of any nation's efforts to improve its productivity must be a commitment to invest in plant, equipment, and new technology. Yet, compared to the efforts of our economic competitors, American capital formation is inadequate. We have encouraged consumption at the expense of savings and investment, much of the available financing is diverted unproductively, and our financial markets are directed toward short-term profits at the expense of long-term productivity improvements. Most surprising of all in the country with the most sophisticated capital markets in the world, we found that few mechanisms exist to help the average American invest in small firms—the firms that have created most of the new jobs in the last 20 years.

Despite isolated efforts, most students appear to leave school underinformed—even misinformed—about economic matters.

- **Savings.** The American savings rate ranks last among industrialized nations. Other nations, including West Germany, Canada, and France, save and invest far more than we; Japan saves nearly four times as much. The growth of the United States federal deficit in the last six years has absorbed about 50 percent of the private sector's normal savings.
- **Cost of Capital.** By international standards, the cost of capital to American business is extremely expensive. Recent analyses indicate that capital is twice as expensive in America as in Japan, a competitive burden to American business at least equal to the cost of American wages and salaries.

- **Use of Capital.** Last year was the third consecutive year in which corporations raised as much debt to finance mergers or protect themselves from raiders as they raised to invest in new equipment, facilities, and financial assets.
- **The Narrow Base of Capitalism.** Very few Americans purchase stock. Although millions own stock indirectly through Individual Retirement Accounts, pensions, insurance, and mutual funds, only seven percent of our people own stock directly.
- **Capital Unavailable to Small Business.** Witness after witness told the Commission about the lack of long-term capital for small business. They pointed to legal restrictions prohibiting major institutional investors, including the managers of pension funds and IRAs, from investing in small firms. They also emphasized that capital for minority enterprise was a particular difficulty.

The American savings rate ranks last among industrialized nations.

- **Aging Equipment.** Seventy percent of the manufacturing equipment in the United States is ten years old or older, compared with only 40 percent in Japan.
- **Consumer Debt.** Consumer debt in America, excluding mortgages, exceeds $575 billion — triple the level of a decade ago — a phenomenon encouraged until only recently by policies that both taxed interest on savings and permitted deductions of interest on loans.

Analysts reviewing these data have come to sobering conclusions. Professor Bruce Scott of the Harvard Business School told the Commission that the United States has been losing its capacity to compete in the world economy and that America "leads the world in consumption, is last among the industrialized nations in savings, and is well on its way to becoming the biggest debtor ever."

Economist and business owner George Hatsopoulos provided a similarly grave warning: "A dramatic and frightening change is underway, which must be addressed before our bubble bursts.... If our competitors invest three times as much per worker as we do, we will lose jobs, our productivity will decline, and they will take markets away from us."

Problems of the Small Firm

The inadequate capital environment in the United States

creates difficulties for all businesses, but particularly for the small firm.

- **Venture capital.** The Joint Economic Committee of Congress reports that many worthwhile proposals cannot be financed. All across America, small business men and women report that venture capital is largely unavailable for new firms. According to the Joint Economic Committee, "Only the cream of the crop of entrepreneurial investments receive funding from the venture capital community."
- **Long-Term Financing Difficult.** Established small firms can obtain only short-term financing from local banks—often at high interest rates. Most small firms report a total lack of long-term funds, i.e., money for 60 months or longer.
- **Bias Against Small Business Investment.** Congressional surveys report a "bias" against small business investment on the part of the financial community, stemming in part from a misunderstanding of small business, the difficulties of administering a loan portfolio with many small loans, the prohibitions against financial institutions holding an equity position in the companies of their borrowers, and the lack of a developed secondary market to recycle small loans.
- **Raising Equity.** Securities regulations, though recently simplified for small business, are still cumbersome, and the process of offering stock is so expensive for small issues that many small firms find it easier to raise equity on foreign exchanges.
- **Impact on Minorities.** These problems are nearly insurmountable in minority communities, most of which lack the resources the small business owner needs, especially the pool of capital that family and friends can provide.

Urgently needed . . . are new mechanisms and financial instruments to increase the volume of capital investment in small firms.

It is impossible to avoid the conclusion that the capital needs of the small business owner have been largely ignored by the institutions that dominate banking and finance, as well as by those who make policy governing those institutions. This situation was easier to understand when the country could rely on great corporations for its economic growth, and when banking institutions were naturally attracted to the efficiencies of large financial transactions. But self-sustaining

Tax Reform Act of 1986

The Tax Reform Act of 1986 represents a major restructuring of the federal income tax system. The legislation reduces the top tax rate for most individuals to 28 percent, and reduces the top corporate tax rate to 34 percent. It is estimated that the Act will reduce the tax burden on individuals by approximately $120 billion over the next five years, while corporate taxes increase by a similar amount.

Among the new law's major provisions relating to business are these:

- Reduction of the top corporate income tax rate from 46 percent to 34 percent.
- Elimination of the provisions for long-term capital gains for both individuals and corporations. The maximum individual capital gains rate will rise from 20 percent to 28 percent for most taxpayers. The corporate capital gains rate will rise from 28 percent to 34 percent.
- Elimination of the investment tax credit (ITC), now worth up to ten percent of the cost of machinery and equipment, retroactive to January 1, 1986.
- New, longer depreciation schedules for writing off investment in plant, machinery, and equipment, meaning smaller deductions each year.
- Extension of the Research and Development tax credit through 1988 with a reduction in the value of the credit from 25 to 20 percent.

prosperity is no longer possible if inventors, entrepreneurs, and even mature small firms are left to struggle to find their financing.

Urgently needed, in the Commission's view, are new mechanisms and financial instruments to increase the volume of capital investment in small firms. When the country recognized the importance of expanding housing and student loans, financial institutions and the federal government together created the necessary financial vehicles. Those precedents can serve as models to help provide small firms with investment capital while covering investors' risks, providing a reasonable rate of return, and offering the liquidity that small investors require.

The Reluctant Exporter

Although the Department of Commerce estimates that each $1 billion in expanded exports supports nearly 25,000 domestic jobs, we do little to encourage small firms to export.

Improving this situation requires our society to take up a formidable agenda:

- **Few Exporters.** Only ten percent of American firms export, and just 250 companies account for nearly 80 percent of the dollar volume of American exports. An estimated 30,000 small firms provide exportable goods and services; in fact, these firms export nothing at all because for many of them foreign markets are the invisible option. Efforts by national and state government to identify, reach, and serve these firms are, according to testimony before the Commission, "notably deficient."

Only ten percent of American firms export. Just 250 companies account for nearly 80 percent of the dollar volume of American exports.

- **Export Decline.** Between 1980 and 1982, in the depths of the recent recession, small business experienced an absolute decline of 15 percent in real exports, twice the decline of all U.S. exports. We might anticipate that further erosion of American competitiveness will strike these firms first.
- **Lack of Government Assistance.** Only one percent of the Small Business Administration's loans were used for exporting between 1983 and 1985, and no export loans were made in 1986. Eximbank, which provides federal

support for the sale of American products abroad, has not used the full amount of loans and guarantees for small firms authorized by Congress.

- **Too Many Agencies.** The bewildering array of official agencies is a problem in its own right. The U.S. Foreign and Commercial Service in the Department of Commerce provides useful information on foreign markets but cannot provide export financing. Those agencies with the financing available appear unwilling to provide it to small firms. The recent enactment of legislation authorizing Foreign Sales Corporations (FSCs) and Export Trading Companies coincided with fluctuations in the value of the dollar and growing interest in tax reform, leaving both mechanisms in limbo.

At the same time, foreign business owners enjoy official support that "turns me green with envy," one small exporter told the Commission. Sponsorship of trade delegations abroad, assistance with shipping and letters of credit, joint ventures to spread risk, certain tax preferences, as well as financing to cover pre-export costs and collecting receivables are all perfectly acceptable under the General Agreement on Tariffs and Trade (GATT). For a variety of reasons, such mechanisms are largely unavailable to the American business owner.

Obstacle Course for Growth and Competitiveness

The most fertile environment for business growth and vitality encourages entrepreneurial risk and minimizes barriers to expansion. But the environment in which businesses operate today falls short of that standard. Businesses are, in fact, hampered by two sets of conditions—one self-generated and the other external. Both choke growth. On the one hand, our economic health depends on business policies and procedures

Within business . . . outdated and internally contradictory perspectives stifle initiative and reward playing it safe.

that encourage growth and risk-taking. Instead, within business, we find outdated and internally contradictory perspectives that stifle initiative and reward playing it safe.

Legislation, regulation, and litigation, on the other hand, add

to the cost of American goods and services. These difficulties make business decision-making more complex, seriously hindering innovation and expansion. The Commission understands that such issues as environmental and occupational safety, consumer protection, and the integrity of financial markets are important national goals. Nevertheless, we believe it is possible to achieve them without a maze of agencies and red tape.

Ironically, the things that make profits possible in the long run are being sacrificed to the cosmetics of a short-term outlook.

These two sets of conditions have combined to create a climate which itself threatens the dynamic nature of American business and impedes its ability to compete:

- **Political Difficulties.** Government seems unable to deal effectively with the major economic issues of our time: the budget and trade deficits, the value of the dollar, inflation, unemployment, the cost of capital, and regulation. The political process itself often has difficulty discerning where the public interest lies in the welter of conflicting claims and counterclaims.
- **Myopic Management.** The necessity to replace plant and equipment, to invest in a productive workforce, and to produce quality goods at competitive prices has too often been ignored by management. Ironically, the things that make profits possible in the long run are being sacrificed to the cosmetics of a short-term outlook.
- **Difficult Labor-Management Relations.** Although the leaders of many unions and industries have responded to the imperative to improve labor-management relations, more action is needed. Both labor and management must cooperate to produce a healthy, competitive economy.
- **Clogged Courts.** The law is changing so rapidly that most business owners understand neither their obligations nor their rights. It takes years to resolve even the simplest matters in our courts; judgments in ordinary tort cases are less and less based on fault and more and more on the depth of the defendant's pockets.
- **Liability Insurance.** The insurance crisis has reached alarming proportions. Premiums and judgments have skyrocketed. Different states apply different criteria in tort

cases. Important public purposes ranging from job creation to environmental control are threatened as business owners hesitate to take advantage of markets in which litigation is to be expected.

- **Limited Information.** Information in the modern age is indispensable. But the official data available to the business owner are seriously flawed. The government collects mountains of information but much of it is not readily accessible; most is not timely; and useful information about foreign markets is lacking. Ignoring the rapidity of change, the government continues to collect data describing a vanishing industrial past. For example, we can compute the number of workers sewing buttons on shirts, but we cannot pinpoint the number of computer salesmen.

- **Banking Turmoil.** American financial institutions can now engage in a wide variety of activities abroad that are prohibited in the United States—including underwriting corporate securities. The recent deregulation of London's financial markets promises to accelerate this development.

In sum, the business landscape is scattered with hurdles to initiative, imagination, and innovation. These obstacles stifle growth and undoubtedly add to the cost of American goods and services on world markets. The success of small firms in recent years demonstrates their ability to cope with these difficulties. Nonetheless, evidence before the Commission clearly showed that too much time and energy is misspent dealing with "the system" instead of with business.

Recommendations

In light of the need for action, the Commission has agreed on five recommendations. The difficulties we have defined, though severe, are not insurmountable. The major task lies in forging the national will to respond to the competitive challenge before us.

The recommendations of the Commission serve three broad purposes. First, they outline institutional mechanisms to focus sustained attention on the problems we have discussed. In this regard they are but the first steps in a continuing and difficult process. Second, they suggest some immediate actions to improve our economic performance and particularly, to utilize an asset that has, until now, been largely ignored—small business. Finally, the Commission hopes to define some common ground on which the leaders of industry, small business, government, education, and labor can agree.

The recommendations serve as suggestions for what we need to do, not as rigid guidelines for how to do it. As such, they represent a starting point for productive debate.

Recommendation A

Mobilize Our People

We recommend a major effort, engaging the attention of public and private leaders nationwide, to alert Americans to the realities of the new world economy, to improve public understanding of our economy and the role of enterprise in it, and to emphasize Americans' opportunities for full employment through creative participation in the nation's economic life as entrepreneurs, business owners, and employees.

Implementing Recommendations

1. Public Leadership. Elected officials should take the lead in developing, sponsoring, and articulating the message about the basic elements and dynamics of the new world economy to our people. Specifically, all governors should lead an examination of the effects of international competition within their states, including attention to its impact on jobs and on small firms. Local officials should foster a fertile climate for small business and employment growth, encouraging new firms to start and existing firms to expand. Federal officials should insist that issues of employment and competitiveness remain high on the national agenda and should marshal the political will and confidence of our people to respond to the tasks before us.

2. Private Sector Leadership. Unions, corporate executives, business owners, and their trade associations should increase their efforts to inform their employees and members of the issues described in this report. We urge corporate and union leaders together to develop educational initiatives to inform the workforce of company plans and prospects for the future and to stress each employee's personal stake in the global economy.

3. Public Understanding. In light of the extraordinary importance of these matters, the President should deliver an annual message to Congress on improving the nation's competitive position and expanding employment opportunities for the American people. Communications leaders in newspapers, magazines, television, and radio should provide more and better analyses of issues relating to the health of the American economy.

4. Education. Each state board of education should act to insure that today's students are prepared to function in tomorrow's world. The study of foreign languages and cultures is essential, as is a solid preparation in modern history,

current affairs, and world geography. Social science and economics are also important if our young people are to understand the values, dimensions, and benefits of our economic system. In this effort, particular attention should be paid to the quality of teaching since so few schoolteachers themselves understand the dynamics of our economic system. All prospective teachers should study economics.

5. Education for Opportunity. Those who dream of creating a business need the skills to run one. Every state should review the educational offerings of its schools—in particular, its vocational programs in secondary schools and community colleges—to make available training in business creation, including business and financial planning, cash flow management, employee development, and managing and consolidating growth. Efforts should be made to involve small business owners in developing these curricula as well as in teaching.

Recommendation B

Prepare Our Workforce

We recommend national efforts to: (1) provide workers and managers with the skills required to compete in and adapt to the new business environment; and (2) develop the flexibility needed to begin new roles, even new careers, in a changing economy.

Implementing Recommendations Regarding Skills

1. Early Learning. Today's infants will be the entry-level employees of the 21st century. Educational research demonstrates convincingly that uncorrected early learning deficiencies are compounded with the passage of time. We believe that to help assure a productive and competitive workforce, every community should provide stimulating preschool learning environments, available on a voluntary basis, and more rigorous elementary school education to prepare students for high school.

2. Educational Standards. Implementation of the recommendations for more rigorous school standards for students and teachers of the National Commission on Excellence in Education and of the Carnegie Forum on

Education and the Economy is essential and long overdue. Following through on these reforms will lead to American workers, managers, and teachers who are more skilled, more adaptable, more conscientious, and better prepared for the world of work. We urge business leaders to set aside time to work with local schools and colleges in support of these efforts. Many tasks need attention: guest lecturing, volunteering for education task forces, hosting visiting student groups, and other activities that create business-education partnerships.

3. Mathematics and Science. The pressing need for improved mathematics and science instruction to upgrade the technical skill of our workforce must be addressed by efforts such as: (a) stronger requirements for course completion for high school and college graduation; (b) salary supplements to attract more able teachers of mathematics and science to our secondary schools; (c) grants and forgivable loans to encourage undergraduates to pursue careers in science, mathematics, engineering, and teaching; and (d) magnet schools for particularly talented students in math and science.

4. Colleges and Universities. Public and private colleges and universities, including community colleges, have an extraordinary array of resources that can assist local, state, and regional economic development. We recommend that each educational institution work with local public, business, and labor leaders to decide which of the following resources it can best provide:

- research and analysis,
- training programs,
- technology transfer efforts,
- entrepreneurial institutes, or
- centers of excellence in areas of outstanding faculty strength.

Implementing Recommendations to Encourage Flexibility

1. Training and Retraining. Private and public efforts to train, retrain, and enhance the skills of employees need to be expanded. We recommend: (a) business support for educational leave and tuition reimbursement for employees' educational expenses; (b) amending existing public job-training programs to encourage local public agencies to place participants in internships with small business; (c)

carefully designed and managed employment opportunities in the public sector, accompanied by mandatory education and training, that will provide job experience for poorly skilled entry-level workers and encourage regular work habits.

We have an obligation to create jobs that offer a future of self-development—jobs that are not merely life sentences to drudgery.

John Sloan
National Federation of Independent Business

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2. Employers and Training. Because U.S. employees frequently change jobs, employers are less inclined to sponsor training and retraining. Federal and state governments should encourage business investment in employee development through special tax or other incentives.

3. Individuals and Training. Existing individual exemptions for employer-financed education and training, scheduled to expire in 1987, should be maintained and made permanent. Many economists and business leaders have suggested that businesses cooperate with their employees to establish individual training accounts, similar to Individual Retirement Accounts, as a mechanism for upgrading skills and developing new ones. We believe this idea, including the possibility of tax deferrals on contributions and on the interest they earn until used, is worthy of serious exploration and experimentation.

4. Portable Pensions. In the new economy, where career change is a constant, the pension structure must be simplified to enable employees to plan their retirement security. The first step is to accept the principle of a pension that travels from job to job and employer to employer. Varying structures for implementing this principle have been proposed; all have merit. It is time to act on the principle.

Recommendation C

Invest In Our Future

We recommend doubling business investment in plant, equipment, and technology in the next five years. Special attention should be given to providing small firms with new streams of capital and to promoting "people's capitalism" to enable more citizens to take a stake in the success of American business as equity holders. Critical to reaching these goals are instruments and mechanisms to provide liquidity, safety, and a reasonable return on investment to investors.

The incentives proposed below include encouraging greater national savings; improving investment credits; expanding stock ownership, especially equity participation in small business mutual funds; encouraging research, development, and technology transfer; increasing state efforts to assist small business; and encouraging business formation in distressed areas. These proposals offer no special advantages for small business. They are designed to erase the obstacles faced by small business in our capital markets—obstacles that have already been removed for other larger users of capital.

Implementing Recommendations

1. Savings. Net national savings—the sum of private and public savings, less public deficits—must be increased by encouraging greater personal saving and by reducing the federal deficit. We believe that national policy should encourage people to save and that reducing the taxation on savings is sound public policy. We consider it essential that federal revenues and expenditures be brought into balance at approximately 20 percent of the gross national product.

2. Reestablish the Investment Tax Credit. We recommend reestablishing the Investment Tax Credit. We believe the credit should be focused to make it more useful to small business and that the potential for abuse of the credit can be minimized if it is directed at machinery and equipment essential to improving productivity.

3. Holding a Stake in American Prosperity. We recommend linking the success of American business to the direct financial interests of the American worker by democratizing financial markets and permitting far more citizens of moderate means to acquire an equity stake in business. Specifically, we urge:

- Structuring benefit programs that encourage employee participation in investment funds. Numerous well-managed and successful thrift plans already exist to serve as models.
- Expanding opportunities for profit sharing and employee stock ownership for American workers. The systems required include routine consideration of such opportunities during company reviews of benefit programs, financial mechanisms to help employees gather the capital they need on terms they can meet, and disinterested, expert assistance in analyzing the merits of employee ownership.

4. Small Business Mutual Funds. We recommend the establishment of small business mutual funds in the private sector, to direct substantial capital investment into job-creating small businesses. We strongly recommend that new mechanisms be created so that major sources of savings and capital—pension funds, IRAs, insurance companies, and trusts—can prudently invest substantial assets in small businesses. The necessary mechanisms include: protecting against loss through self-insuring set-asides; providing an attractive rate of return including participation in equity growth; and offering investor liquidity.

In the next five years, robots may replace over seven million manufacturing jobs.

Lawrence Crockett
Institute of Science and Technology
University of Michigan

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5. Public/Private Partnerships for Small Business Investment. Federal, state, and local governments should join in partnership with the private sector to significantly increase the volume of long-term, fixed-rate, small business loans. Specifically, we recommend:

- Improving the existing small secondary market for small business loans to make it comparable to existing markets for student and housing loans. A more vigorous secondary market can be created if the federal government: (1) encourages financial guarantors, including insurance companies and bank holding companies, to provide loan insurance to small firms; and (2) reinsures these insured loans against catastrophic loss.
- A federal-state guarantee program, similar to federal-state housing coinsurance, to encourage states to coinsure federal loans, thus permitting the federal government to

reduce its exposure to 50 to 70 percent of each loan.

- A primary loan guarantee program combined with greater lender discretion and accountability, directed at newer firms and women- and minority-owned businesses. We believe the federal guarantee for these loans might be as high as 90 percent.

The truth is, as far as any small business owner is concerned, the capital markets in this country just don't exist.

Sara Loveland
National Development Council
New York, New York

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6. Encourage Long-Term Capital Investment. The tax structure should encourage long-term private investment for growth and reward the assumption of risk. Several analysts, for example, have suggested indexing capital gains taxation by the number of years the investment is held as well as granting more favorable treatment for long-term investments in small firms. At a minimum we consider the following essential:

- Long-term investment in productive assets should be encouraged by taxing gains from such assets held over a five-year period at a rate lower than the rate for ordinary income, with consideration given to a yet more favorable rate for investments in new or smaller companies.

- Investment in "illiquid" new and small companies should be encouraged by reducing arbitrary barriers to equity investment. For example:

  —Subchapter S of the Internal Revenue Code is a desirable form of incorporation for many small firms but it is restricted to businesses with not more than 35 individual shareholders. We believe the permissible number of shareholders should be increased to 100 and that venture capital funds should be permitted to invest in these corporations.

  —The Securities and Exchange Commission in 1982 adopted "Regulation D" governing small offerings of private securities. More onerous state requirements should conform to the SEC requirements.

  —Pension fund "prudent investor" rules are essential. We believe they should be applied to a pension's entire portfolio, and that federal "plan assets" requirements

should encourage pensions to invest between one and three percent of their assets in new and growing companies and in venture funds.

—An Inflation Index should be developed so that capital assets held for the long term can be indexed in order to tax investors on the basis of real economic gain, not on the basis of inflationary gains.

7. Research, Development, and Technology Transfer. We recommend:

- Increasing public and private support of university-based research, development, and graduate education.
- Increasing the highly successful Small Business Innovation and Research Program (SBIR) to three percent of existing government research and development expenditures.
- Creating, in every state, support systems for technology transfer that encourage partnerships between the academic and small business communities. Such partnerships can help commercialize university-based research and development and serve as a forum to introduce academic engineers and scientists to their counterparts in small technology-based firms.

Tiny Asian sewing shops have devastated American garment industry giants. . . .

Erwin von Allmen
W.C. Smith Inc.
Philadelphia, Pennsylvania

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8. Partnerships for Job Creation. States should provide incentives for insurance companies, banks, bank holding companies, savings and loans, pension funds, and foundations to create private, state-chartered partnerships to focus on job creation through investment in "targets of opportunity." Targets could include biotechnology, robotics, CAD-CAM (computer-assisted design and manufacturing), small manufacturing, community-based housing and entrepreneurship, and programs for training displaced workers, minorities, women, and other entrepreneurs new to the mainstream. Job creation should be a fundamental goal.

9. Incentives for Independence. Government efforts to provide public assistance and unemployment compensation must be complemented with efforts to encourage

self-employment and entry into the labor market. Experiments should coordinate a variety of services required to obtain and keep a job, including education and training, child care, transportation, nursing care for home-bound relatives, and other aids to employment and self-employment. Such experiments can succeed, however, only if participants continue to receive benefits at least during the initial stages of the transition.

10. Experimentation. State and private leadership is needed to establish small business incubators, enterprise zones, community development corporations, and other experiments to encourage business creation and expansion in distressed urban and rural areas. Federal efforts in economic development should support these innovations and encourage local initiatives that respond to local problems.

Recommendation D

Restore the "Yankee Trader" Tradition

We recommend continuing the policy of the United States that supports the fair trade of goods and services among countries, combined with an aggressive, visible, high-priority program to restore a vigorous, exporting industrial base that will include large numbers of smaller firms.

Implementing Recommendations

1. Expanding GATT. The United States should continue its emphasis on including services, intellectual property rights, and agricultural products in the scope of the General Agreement on Tariffs and Trade (GATT).

- The U.S. Trade Representative, in the current negotiations, should seek GATT recognition of the economic burden the United States bears in assuming a major share of the defense costs of most of our trading partners in Europe and the Pacific Basin.
- The U.S. Trade Representative, in negotiating GATT terms, should insist that all signatory countries comply with the spirit and intent of the Agreement. Penalties or countervailing procedures should be invoked where violations are found and documented.

2. Import Quotas. Import quotas and voluntary restraints obviously impede trade. Those now on the books should be periodically reviewed. If the quotas or restraints cannot be justified, they should be removed. If found appropriate, quotas and restraints should be enforced and maintained.

3. Expanding Exporting Base. Specific incentives should be enacted to attract new companies into the exporting industrial base and to encourage those already exporting to expand. For example:

- Improve and simplify the Foreign Sales Corporation provision to make it more useful to smaller firms.
- Require Eximbank to market its existing small business export financing programs more aggressively. State governments should strengthen their export financing programs to expand the availability of funds.
- Create a Small Business Exporting Incentive program similar in structure to the existing Small Business Innovation and Research program.
- Seek alternative methods under GATT to allow U.S. exporting companies specific cost reductions through tax incentives to match the tax incentives available to businesses in other countries.

4. Serving Small Business. Improve the education of small businesses in exporting by:

- Working aggressively with states and small business groups to disseminate information concerning programs of the International Trade Administration (ITA) already available to small firms.
- Reorienting ITA export promotion programs to focus specifically on small business participation. Measures of effectiveness tied to expansion of the exporting industrial base, rather than the short-term dollar value of exports, should be applied.

No business today—large or small—can afford not to think of the impact of this globalization trend.

The Honorable Clarence Brown
Deputy Secretary
U.S. Department of Commerce

- Improving implementation of the Export Trading Companies Act by actively assisting the formation of ETCs. We believe that, if the anticipated benefits of authoring

ETCs are ever to be realized, a serious commitment to large ETCs is in order. Other mercantile nations combine the resources of government, business, and financial centers to encourage exports and we can do no less.

5. **Marketing Data.** Improve the flow of marketing data by:

- Developing an International Commerce Business Daily to provide timely marketing leads to small firms nationwide. The publication should be tied into the U.S. and Foreign Commercial Service computer system.
- Creating incentives for multinational corporations to use U.S. small businesses as subcontractors in overseas projects.
- Providing incentives for large companies to assist small U.S. companies abroad by use of facilities and market leads.
- Establishing a public-private partnership to provide market information and analysis to the business community, similar to that provided by the Japanese External Trade Organization (JETRO).

We should not subsidize failure; the bulk of the risk should continue to be on the entrepreneur's shoulders.

Patrick A. Thompson
Trans-Matic
Holland, Michigan

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6. **State Leadership.** Leadership on the part of state governments to encourage exporting is essential to take advantage of the considerable economic power of individual states and the closeness of state governments to small firms. We believe every state should set a goal of increasing small business exports by ten percent annually. Working with Department of Commerce regional offices, each state should:

- Analyze its own trade flows with other nations to identify both imports of great demand within its own borders and its own products that are in demand overseas.
- Establish promising exchange relationships with representative nations around the globe—one, for example, in the Pacific, one in Latin America, one in Africa, and one in Europe—to help its small firms gain experience in trading, as well as learn the language and customs of different parts of the world.
- Sponsor small business exporting initiatives such as

financing mechanisms, trade delegations abroad, state-sponsored Foreign Sales Corporations, and trade missions.

7. A Conference of Summit Nations on Small Business. The economic summit nations should build on their 1986 statement that technological innovation and small business expansion are the keys to non-inflationary economic growth by organizing an economic summit conference on small business and trade. We recommend that the President of the United States and the leaders of the other summit nations convene such a conference between 1990 and 1992 that would:

- put small business owners around the world in touch with each other;
- encourage American business owners to learn how others organize themselves for exporting;
- permit others to learn how American small business succeeds in our environment;
- provide small business participants the opportunity to understand the development of policy for international trade; and
- open the possibility of greater consideration of small business in GATT.

We believe the 1986 White House Conference on Small Business could serve as a model for such an international conference.

Recommendation E

Clear the Decks

We recommend that the institutions responsible for economic growth in the United States—government, business, labor—reorganize their structures and processes to reflect the new realities of global competition, the imperative to restore American competitiveness, and the powerful role of small business in America in meeting these challenges.

Implementing Recommendations

1. The Test of National Policy. In developing national economic policy for the coming decades, priority should be given to two considerations:

- Does this policy contribute to America's ability to compete in the world?
- Does it support job creation, business expansion, and small business growth?

These tests set a demanding standard. The Commission is quick to acknowledge that even policies which fail both tests might make good public policy; nevertheless, putting the questions should make us aware of the consequences of our decisions.

2. Organizing for Global Competition. In both the executive branch and Congress, trade-related functions must be coordinated, and responsibility for improving our competitive position assigned. With respect to the executive branch, cooperation is essential among the Department of Commerce, the Small Business Administration, the Departments of Treasury, State, Agriculture, and Defense, and the Office of the United States Trade Representative. The President and Congress should either act to create a Department of Trade to unify our trade policy and activity, or the President should devise other means to eliminate bureaucratic overlap, clarify lines of authority, and correct indecisiveness in our trade policy.

The dispersion of responsibility for matters related to international competitiveness among the committees and subcommittees of Congress is also a difficulty. We urge the committees of Congress with jurisdiction over issues related to international competitiveness to exercise keener oversight of these issues in order to keep these matters before the public.

3. Public and Private Cooperation. We applaud the significant private leadership demonstrated in the work of such groups as the Committee for Economic Development, the Business–Higher Education Forum, and the newly-formed Council on Competitiveness. We believe the work of such groups can be complemented effectively by a public–private partnership in the form of a standing body to analyze domestic economic growth and American competitiveness. Congressionally chartered, but privately supported, the Council should include state and local public officials, corporate leaders, financiers, small business owners, educators, and representatives of American labor. Its charge should be to assess American competitiveness, including the impact of government regulations, the health of small business, the adequacy of government data, and the effect of legislation and judicial decisions on the economy. Of special concern in the immediate future is assessing the consequences for economic growth of the tax legislation of 1986.

4. The Budget Process. The monumental accomplishment of the 93rd Congress in creating a Congressional budget process

can be improved by the 100th. More specifically, biennial, as oppposed to annual, budgets should be developed to provide budget makers with more time to refine their projections. A biennial budget would grant authorizing and appropriating committees greater discretion and lead time in meeting budget guidelines. A two-year budget cycle would also give the business community a better sense of the government's outlook for the next 24 months.

5. Liability Reform. The liability insurance crisis must be resolved. The elements of a solution seem to include:

- Acknowledging that the hazards of everyday living will always be among us.
- Returning to a fault-based standard of liability.
- Continuing punitive damages in cases of deliberate corporate misconduct; amounts awarded should be divided equally between plaintiffs and an appropriate state agency or program.
- Establishing nationally uniform product and commercial liability standards, including liability based on scientific knowledge at the time of manufacture, not at the time of injury.
- Limiting attorneys' contingency fees.
- Developing standards for insurance companies to disclose the terms and conditions of their portfolios and their lines of insurance. The insurance industry should do so itself before the government is forced to step in.

Every problem should not require a legal remedy.

Bruce Bunner
Insurance Commissioner
State of California

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6. Small Business and Taxes. The House Ways and Means Committee and the Senate Finance Committee should analyze the impact of all new tax legislation on small business. These analyses should include statements of the assumptions, rationales, and data underlying the analyses.

7. Streamlining Procedures. State and local governments should streamline the many procedures governing the establishment and operation of a business. We believe that a single office responsible for helping entrepreneurs and small businesses complete the paperwork requirements for getting started can be helpful. These offices can also serve as both

ombudsmen and advocates for small business.

8. The Small Business Administration. The Small Business Administration has evolved over 30 years in response to the needs of the small business commmunity. Despite the limited resources at its disposal in the face of sweeping responsibilities, the SBA has made significant contributions to small business through its creation of the venture capital network and of certified local development companies, as well as its loan guarantee programs, management assistance, and advocacy. We believe this record should be respected, and that the SBA, without diluting its mission or independence, can be made more effective by:

- refocusing its lending efforts to help develop the systems, institutions, and credit instruments needed by the small business community;
- exerting ongoing, not sporadic, leadership to help states and localities focus on small business as a foundation of their economic development; and
- expanding and improving SBA's advocacy role for small business, including its ability to analyze small business growth.

I want to pay my fair share of taxes but I cannot plan growth intelligently when taxing policies are so volatile.

Earl Hess
Lancaster Laboratories
Lancaster, Pennsylvania

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9. Labor-Management Relations. We recommend a White House conference on labor-management relations to help encourage a positive culture for business development and employee relations. The White House can direct the nation's attention to the imperative for new ways of thinking about the relationships between business and labor in the new competitive environment. We need partnerships between management and labor, taking into account new management styles and changes in employee expectations. Such innovations as more joint planning and diagnosis, work teams, task delegation, reconciling seniority with ability, pay differentials, and training incentives should be considered.

A Competitive People

A competitive people defines itself in the challenges it meets—and overcomes. In former years, Americans passed

that test on the frontier, in the crucible of political and industrial revolutions, and in the necessity of battle. In our own time, we have pushed back the boundaries of science and technology.

Now another challenge lies before us—pursuing our national aspirations in the context of the new world economy. We believe that today's Americans are up to the task. Made aware of the dimensions of the problem, they will work as hard as those who tamed the wilderness, they will save as much as those who financed World War II with war bonds,

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Indians like to think they can soar like eagles. Entrepreneurship permits us to maintain that vision.

Robert Powless
President
Mount Senario College

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and they will learn what they need to know in order to participate productively in the economic struggle we face.

In taking up this challenge, we have little tolerance for those who counsel patience. To those who point to every imaginable excuse to explain the American decline, we say our country has lost world market shares in good times and bad, on the back of a strong dollar and a weak one. We agree that the growth of services and information industries is significant and must be maintained, but we insist that an America stripped of its industrial and manufacturing foundation is inconceivable. The Commission has no desire to deny to the people of other lands the higher standards of living and material well-being their economic success deserves; but we are equally convinced their success does not require us to sacrifice the well-being of American workers and families.

Nor is the Commission's conviction about the importance of small business to be interpreted as lack of concern while one great American industry after another falls before foreign competition. Reversing the decline in the fortunes of our large corporations is a compelling national need and critically important to the many small firms which provide the products, parts, and services to our nation's industries.

We call on all who care about our future to step forward to meet this latest in a long line of challenges. All will be tempered by it; none will be untouched by it; mastering it will be the making of our future.

To our public officials: We urge you to take seriously the findings in this report and to respond promptly by enacting the recommendations that fall within your areas of

responsibility. Of particular importance is your steadfast commitment, in the face of short-term pressures from all sides, to the long-term interest of American competitiveness.

To our citizens, including parents, students, and employees: Act now on the realization that the traditional structure of employment and job security is becoming a thing of the past. Honing individual skills will give each of us a competitive edge in the future.

To our corporate officials: We remind you that the freedom to engage in business carries with it the obligation to lead, to respond to the public interest in making decisions about plant locations and investment opportunities. Most important, your actions must affirm, not undermine, the dignity of employment. You have a special responsibility to take seriously the imperative for retooling, marketing abroad, controlling costs, and thinking strategically for the long haul rather than tactically for the short.

To our financiers and bankers: You have a central role to play in creating the financial processes and instruments that will, in partnership with the public sector, promote foreign trade, encourage small business expansion, and lead business owners to productive participation in these efforts.

To our labor leaders: Share with the members of your unions your realization that the welfare of your members depends on a competitive economy. Just as collective bargaining has been the heart of trade unionism in the past, productivity will be its soul in the future.

We speak finally to our small business men and women, the owners and entrepreneurs who have carried the American workforce safely through the difficult last decade: Maintain your belief in yourself. Build on your accomplishments. Push back your horizons. Above all, hold fast to your dreams, remembering that they sustain not only you but all of us.

Appendices

Appendix A

Acknowledgments

Many people and organizations made the work of this Commission possible; we cannot overstate the value of their contributions.

The Commission wants, in particular, to acknowledge its debt to the following:

- The 38th and 39th Presidents of the United States who lent us their support.
- The 18 members of the House and Senate who conceived of the Commission and saw it to fruition.
- The Charles Stewart Mott Foundation, Flint, Michigan, which provided the initial financial and conceptual support for the Commission and more than half of its financial resources. Jack Litzenberg of the foundation's staff, assisted by Ruth Goins, was an unfailing source of encouragement during the Commission's existence.
- The Andrew W. Mellon, John D. and Catherine T. MacArthur, and Rockefeller foundations as well as the Carnegie Forum on Education and the Economy of the Carnegie Corporation of New York, which also provided essential financial support to our efforts.
- Many organizations and institutions which provided us with meeting space, logistical, and other support to help extend the Commission's resources, including the Gerald R. Ford Library, Ann Arbor, Michigan; the Carter Center of Emory University, Atlanta, Georgia; the Bank of America, San Francisco, California; Federal Hall National Memorial, New York City; Rainier National Bank, Seattle, Washington; Control Data Corporation, San Antonio, Texas; the Chamber of Commerce, San Francisco, California; and the New York Stock Exchange.
- The many organizations representing small business that provided us with the benefit of their experience and knowledge, including the U.S. Chamber of Commerce, the National Federation of Independent Business, Small Business United, the National Association of Women Business Owners, the National Association of Small Business Investment Companies, the Small Business Administration, the White House Conference on Small Business and its staff, the Corporation for Enterprise Development, and the National Small Business Association.

- The witnesses and experts who, often at great expense to themselves, eloquently made their cases before the Commission.
- The businesses and organizations from which the Commissioners were drawn, and which supported their time and often their expenses in pursuit of this public endeavor, including the National Development Council, the Bank of America, the AFL-CIO, AT&T, Pacer Systems, Inc., Price Waterhouse, King & Spalding, the American Enterprise Institute, Alexander Haagen Development Company, and the National Business League.

We are especially grateful to Price Waterhouse, the A. Gary Shilling Company, New York University, and the AFL-CIO for the expert assistance members of their staffs provided the Commission. Robert Haddad of Price Waterhouse explored the idea of a mutual fund for small business. Roger Fulton of the Shilling Company provided a comprehensive report on economic developments affecting small firms and drew the declining purchasing power of American families to our attention. Lynne Brown of New York University attended many of our meetings and offered numerous suggestions for structuring and improving this report. Markley Roberts of the AFL-CIO proved an inexhaustible source of information and a careful and constructive critic of the report as it developed.

The Commission also wants to express its appreciation to the staff which helped it throughout its work. Alisa Pittrizzi, Audrey Gallagher, Satura Bridgewater, and Christine Gresock, at different times, helped organize our work.

In particular, we note the invaluable contributions of Kevin Urquhart: without his able and efficient help throughout, we would never have had meeting or hotel space, adequate travel arrangements or notice of meetings, nor have been able to expect prompt and cheerful turnaround on constantly changing agendas and report drafts.

We are indebted also to two consultants: Anne Paxton and Andrea Haines. Ms. Paxton provided summaries of each of the Commission's meetings as well as two newsletters reporting the Commission's work. Ms. Haines developed Appendix B, prepared the Commission's archives, and played an indispensable role in providing research assistance to the Commission.

Finally, we express our gratitude to two small firms that helped prepare this volume: Wordsmith, Inc. and Moonstruck Graphics, both in Virginia. Bruce Boston of the former proved a talented writer and editor, and Dan and Vicki McQuillen, of the latter, designed this report.

Appendix B

Annotations

A Debtor Nation

On September 14, 1986, Clyde Farnsworth wrote in *The New York Times*, "(After) serving as the world's creditor since World War I, the United States this year became the world's largest foreign debtor, overtaking Mexico and Brazil.... Because an increasing portion of America's wealth must go to pay the mounting foreign debt, the huge deficits threaten to lower living standards in this country."

Net U.S. International Position 1982-1985

(billions of dollars)

1982	+138.2
1983	88.5
1984	4.4
1985	-107.4

Source: Department of Commerce, Bureau of Economic Analysis, *Survey of Current Business*, June 1986.

In June 1985, a major publication of the Department of Commerce (*United States Trade: Performance in 1984 and Outlook*) anticipated the reversal of the U.S. international position:

"The recent large U.S. trade deficits demonstrate that the United States has been consuming significantly more than it is producing and borrowing abroad to make up the difference.... Sometime in 1985 the United States will officially become a net debtor nation for the first time since 1914. In other words, the United States will owe more to foreigners than they owe to the United States.... This would represent an enormous swing... in the U.S. net international position—from largest creditor nation to largest debtor nation—in only four years.

"This foreign debt will have to be serviced. The United States will become a net interest payer to foreigners, rather than a net interest recipient. Moreover, at some point, foreigners will no longer be willing to continue enlarging the U.S. net debtor position. At that point, the United States will have to switch from consuming more than it produces to consuming less than it produces in order to make interest payments on the debt. That is, a portion of what is produced in the United States will not be available for domestic consumption or investment but will have to be exported to

earn foreign currency to service accumulated foreign debt.

"When this switch occurs, it may have undesirable effects on the availability of investment capital, interest rates, U.S. economic growth, and the U.S. standard of living."

Exports

According to the International Trade Administration, U.S. Department of Commerce (June 1985), the U.S. share of world merchandise exports fell from 18 percent in 1960 to 11 percent in 1984. The President's Commission on Industrial Competitiveness, *Global Competition: The New Reality* (January 1985) reports the same findings. According to the Department of Commerce, U.S. exports of manufactured goods fell from $166.8 billion in 1981 to $162.0 billion in 1985.

The International Trade Administration also reports that the U.S. high-tech trade surplus dropped from $26.6 billion in 1980 to $6.2 billion in 1984. A report prepared for the Joint Economic Committee (*The U.S. Trade Position in High Technology: 1980-1986*, October 1986) predicts that U.S. high-technology trade will show a deficit of about $2.6 billion in 1986.

Agricultural trade accounts registered a deficit in May, June, and July of 1986, according to the International Economics Division of the Department of Agriculture (October 1986).

Productivity

American output per hour of all persons increased, on average, 2.4 percent in the 1960s, 1.1 percent in the 1970s, and 0.8 percent from 1980-1985 (*Economic Report of the President*, 1986).

Economist A. Gary Shilling attributes the slowdown to the influx of inexperienced baby boomers into the labor force, depressed capital spending, inflation, and, in the 1970s, a decline in the work ethic ("The World Has Definitely Changed," August 1986).

Brookings Institution economist Barry Bosworth concludes that the causes of the post-1973 slowdown "remain, in large part, a mystery" (*Tax Incentives and Economic Growth*, The Brookings Institution, Washington, D.C., 1984, p. 177).

Growth of the Deficit

As the annual federal deficit has increased, so too have the national debt and annual interest payments on the debt.

Federal Debt, Deficits, and Interest Payments 1960-1985

Year	Gross Federal Debt ($ billion)	Annual Surplus (+) or Deficit (-) ($ billion)*	Interest on Gross Federal Debt ($ billion)	Interest as Percentage of Federal Outlays (%)
1960	290.9	+0.3	9.5	8.7
1970	382.6	-2.8	20.0	8.0
1980	914.3	-73.8	75.2	10.2
1981	1,003.9	-78.9	96.0	11.6
1982	1,147.0	-127.9	117.5	13.1
1983	1,381.9	-207.8	128.9	13.3
1984	1,576.7	-185.3	154.1	15.1
1985	1,827.5	-212.3	179.4	15.6

*Includes total receipts and outlays, budget and off-budget.

Source: Office of Management and Budget, *The Budget for Fiscal Year 1987*. Various tables from *Special Analyses* and *Historical Tables*.

Income

Several sources point to declining purchasing power and real (i.e., inflation-adjusted) income for American workers and families:

Average Gross Weekly Earnings for Production and Non-Supervisory Workers in Constant 1977 Dollars

1972	$198.41
1977	189.00
1985	171.60

Source: *Economic Report of the President*, 1986

Index of Adjusted* Hourly Earnings of Production and Non-Supervisory Workers in Constant 1977 Dollars

(1977 = 100)

1972	101.2
1977	100.0
1985	94.3

Source: *Economic Report of the President*, 1986. (*Adjusted for overtime and inter-industry employment shifts.)

Index of Real Compensation* Per Hour for all Workers in Non-Farm Business

(1977 = 100)

1972	95.7
1977	100.0
1985	98.2

Source: *Economic Report of the President*, 1986. (*Hourly compensation divided by Consumer Price Index. Hourly compensation includes employees' wages and salaries and employers' contributions for benefits.)

(See table, P. 51, "Real Average Weekly Wage for Non-Supervisory Workers by Industry.")

According to Harvard's Bruce R. Scott, speaking at the Commission's first meeting, real per capita "spendable" earnings of American workers have been declining since 1972, although "per capita income" has risen. He explains that four factors account for this phenomenon: "increased participation in the labor force, the creation of a large number of low-paying service jobs, dramatic increases in real incomes for those not working (for example those on social security), and the increased fraction of worker incomes absorbed by income and social security taxes." (See Scott, Bruce R., and George C. Lodge (eds.), *U.S. Competitiveness in the World Economy*, Boston: Harvard Business School Press, 1985.)

Loss of High-Wage Jobs

The Bureau of Labor Statistics documents the decline in manufacturing jobs. In 1980, there were 14.2 million manufacturing production workers. By June 1986 the number of such workers had dropped to 13.1 million, for a loss of 1.1 million jobs (Department of Labor, Bureau of Labor Statistics, *Employment and Earnings*, July 1986). Total employment in services rose four million, from 17.9 million in 1980 to 21.9 million in 1985 (*Economic Report of the President*, 1986).

Average gross weekly earnings (current dollars) for manufacturing workers in 1985 were $385.97, about 50 percent higher than the $256.43 weekly earnings for service workers.

(See tables, pp. 52-53, "Full and Part-Time Employees on Private, Nonagricultural Payrolls, 1950–1985.")

Real Average Weekly Wage for Non-Supervisory Workers by Industry
(BLS Report—1967 $)

	Mining	Construction	Manufacturing	Transportation & Public Utilities	Wholesale Trade	Retail Trade	Finance Insurance Real Estate	Services
1973	$151	$177	$125	$153	$120	$ 72	$ 97	$ 88
1978	$170	$163	$128	$155	$117	$ 67	$ 91	$ 84
1984	$162	$147	$120	$141	$111	$ 57	$ 89	$ 81
1985	$160	$141	$121	$140	$111	$ 54	$ 90	$ 81

Source: A. Gary Shilling and Company, "The World Has Definitely Changed," August 1986.

Full and Part-Time Employees on Private, Nonagricultural Payrolls [1] 1950-1985

Year	Total Employment		Goods-Producing Industries [2]			Service-Producing Industries [3]		
	Emp. (000)	Average Weekly Earnings [4]	Emp. (000)	% of Total Emp.	Average Weekly Earnings [4]	Emp. (000)	% of Total Emp.	Average Weekly Earnings [4]
1950	34,349	$133.83	15,440	45	$151.89	18,909	55	N.A.
1960	38,516	164.97	15,653	41	192.11	22,863	59	N.A.
1970	48,156	186.94	17,506	36	225.88	30,649	64	$164.58
1980	60,331	172.74	18,398	30	226.16	41,933	70	149.08
1985	65,911	171.60	17,551	27	232.18	48,360	73	147.49

Source: U.S. Department of Labor, Bureau of Labor Statistics, *Employment, Hours, and Earnings, United States, 1909-1984*, May 1985; *Employment and Earnings*, February 1986; *Economic Report of the President*, February 1986.

1. Includes all production or nonsupervisory employees, but not supervisors, managers, proprietors, executives, the self-employed, or domestic workers.

2. Includes manufacturing of durable and nondurable goods, mining, and construction.

3. Includes transportation and public utilities; wholesale trade; retail trade; finance, insurance, and real estate; and services (e.g., hotels, personal services, business services, auto repair, motion pictures, amusement and recreation, health care, legal and other professional services such as engineering, architecture, and accounting).

4. Constant 1977 dollars. Earnings for goods-producing and service-producing industries calculated by Commission staff according to BLS weighting formulas.

Full and Part-Time Employees On Private, Nonagricultural Payrolls [1]
Selected Industries 1950-1985

	Goods-Producing Industries			Service-Producing Industries					
	Manufacturing			Retail Trade			Services		
Year	Emp. (000)	% of Total Emp.	Average Weekly Earnings [2]	Emp. (000)	% of Total Emp.	Average Weekly Earnings [2]	Emp. (000)	% of Total Emp.	Average Weekly Earnings [2]
1950	12,523	36	$146.80	6,375	19	$100.03	N.A.	N.A.	N.A.
1960	12,586	33	183.48	7,627	20	118.12	N.A.	N.A.	N.A.
1970	14,044	29	208.00	10,046	21	128.66	10,481	22	$150.80
1980	14,214	24	212.06	13,500	22	108.29	15,921	26	140.12
1985	13,215	20	219.93	15,560	24	99.51	19,366	29	146.11

Source: U.S. Department of Labor, Bureau of Labor Statistics, *Employment, Hours, and Earnings, United States, 1909-1984*, May 1985; *Employment and Earnings*, February 1986; *Economic Report of the President*, February 1986.

1. Includes all production or nonsupervisory workers, but not supervisors, managers, proprietors, executives, the self-employed, or domestic workers.

2. Constant 1977 dollars.

Unemployment

Average Unemployment Rate, All Civilian Workers

1950-1959	4.5 percent
1960-1969	4.8 percent
1970-1979	6.2 percent
1980-1985	8.1 percent

Source: U.S. Department of Labor, Bureau of Labor Statistics, in *Economic Report of the President*, 1986.

Automobiles

Hiroyasu Ono, executive vice president of Toyota, estimates that Japanese automakers in the U.S. will produce 1.2-1.3 million cars in 1988, equal to the production of passenger cars by the third-largest domestic automaker in 1984 (Interview, *Journal of Japanese Trade and Industry*, Number 6, 1985). In 1985, the Japanese share of the U.S. domestic auto market was 23.5 percent (*U.S. Industrial Outlook 1986*). The April 22, 1985 *Business Week* includes predictions that all automobile imports will account for 40 percent of U.S. sales by 1990.

Consumer Electronics

The Department of Commerce publication *U.S. Industrial Outlook 1986* documents declines in U.S. manufacture of televisions and radios. Moreover, according to the Department of Commerce, employment in the consumer electronics industry dropped from 76,700 in 1978 to 45,300 in 1983 (*U.S. Industrial Outlook 1986*).

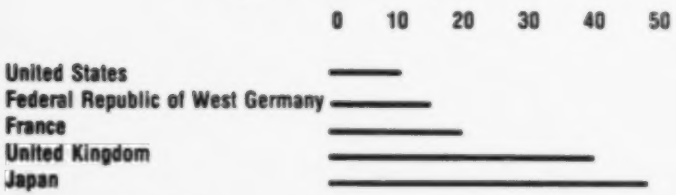
Manufactured Products

Bruce R. Scott and Undersecretary of Commerce Clarence Brown told the Commission at its first meeting that 70 percent of American manufactured products are subject to foreign competition, a situation confirmed by the President's Commission on Industrial Competitiveness (*Global Competition: The New Reality*, January 1985).

In their book, *Subsidies in International Trade* (Washington, D.C.: Institute for International Economics, 1984), Gary Clyde Hufbauer and Joanna Shelton Erb show official export credit authorizations for seven nations. Japan's total exceeds U.S. spending by a factor of four.

A Comparison of Total Exports Supported by Official Finance in the Major Trading Nations in FY 1982

(billions of dollars)



Source: The President's Task Force on International Private Enterprise: Report to the President, December 1984, p. 91.

Steel and Textiles

The U.S. Department of Commerce (*U.S. Industrial Outlook 1986*) reports that imports accounted for 26.2 percent of the U.S steel market during the first half of 1985. The American Iron and Steel Institute reports that the U.S. share of world crude steel output dropped from 131.5 million tons in 1970 to 92.5 million tons in 1984 (*AISI Annual Statistical Report*, 1985).

In 1984 alone, imports of textiles rose more than 40 percent. U.S. imports of textiles and apparel from Hong Kong, Singapore, Taiwan, and South Korea increased from $4.8 billion in 1980 to $9.3 billion in 1984. These countries account for approximately 60 percent of U.S. clothing imports (U.S. Department of Commerce, *United States Trade: Performance in 1984 and Outlook*, June 1985).

Trade Deficits

The *Economic Report of the President* (1986), reports that the U.S. balance of merchandise trade has been negative in all years since 1971 except 1973 and 1975. In constant dollars, U.S. exports of goods and services declined over the period 1980-1984 at a 2.1 percent annual rate, while imports rose ten percent annually. The U.S. current account, the broadest measure of U.S. trade in goods and services, recorded record deficits in the first three quarters of 1986 (*The Washington Post*, December 17, 1986).

The Spirit of Enterprise

There is no single measure of new business formation. Analysts agree that the data on new business incorporations quoted here probably overstate the number of new businesses, since the data include incorporations or internal realignments of existing firms. The Dun & Bradstreet series on business starts reports the number of new entries to

D&B's commercial credit information file, and, since it excludes businesses not in the credit market, may understate the number of new firms. Business starts in the first half of 1986 rose 8.4 percent over the same period in 1985 to 129,035, accounting for an estimated 638,465 new jobs (*Dun & Bradstreet Looks at Business*, September/October 1986).

Average Annual New Business Incorporations 1950-1985

1950-1959	125,024
1960-1969	205,159
1970-1979	365,898
1980-1985	597,736

Source: Department of Commerce, Bureau of Economic Analysis.

Increases in self-employment parallel increases in new businesses. The 1986 small business report of the President shows that the number of unincorporated, self-employed persons increased almost 50 percent between 1970 and 1984. Over the same period, the number of wage and salary workers grew 35 percent, and the civilian labor force increased by 37 percent.

D&B reports that firms with fewer than 100 employees were expected to generate two million of the three million new jobs in 1986. The highest rate of job generation is in the smallest firms (1-19 employees)—they were expected to contribute 31.9 percent of all new jobs in 1986 (*Dun & Bradstreet Looks at Business*, May/June 1986).

Ability to Diversify Economic Opportunity

The information on women-owned businesses was presented to the Commission by the National Association of Women Business Owners. A similar assessment of the progress of women-owned firms is contained in *Small Business in America: The Year 2000 and Beyond* (1986), prepared by the Naisbitt Group for the Institute for Enterprise Advancement of the National Federation of Independent Business. That report also includes figures on Hispanic-owned businesses from the Department of Commerce.

The number of black-owned businesses increased from 231,203 in 1977 to 339,239 in 1982, according to the SBA (*The State of Small Business*, 1986). Because employment in black-owned firms declined slightly over that period, analysts suggest that much of the growth in black-owned businesses represented self-employed entrepreneurs with few or no employees.

A Simple Prescription

Dr. Birch met with the Commission on September 11, 1985. He expanded on his 1981 article ("Who Creates Jobs?" *The Public Interest*, Fall 1981) in which he suggested that innovative small firms are the leading edge of a shift in the American economy from being based on hardware to being based on "thoughtware." In that article he wrote: "Every area in the United States seems to lose jobs at about the same rate, regardless of how rapidly the net job pool is expanding or contracting.... An eight percent loss every year means that half of an area's jobs and establishments must be replaced every five years for the area simply to break even."

Rebecca J. Heflin of the Texas Economic Development Commission testified before the Commission about the job creation task facing the state.

According to the Alabama Department of Industrial Relations (May 1986), Birmingham employment in primary metals declined from 24,200 in 1975 to 13,000 in 1985, while employment in services increased 43 percent, from 53,000 to 81,000.

The Massachusetts data were provided in a 1985 study, "Economic Revitalization and Job Creation in America's Oldest Industrialized Region," by James H. Howell of the Bank of Boston and Linda D. Frankel of the Council for Economic Action in Boston.

Functional Illiteracy

Illiteracy estimates vary greatly. A report by the National Assessment of Educational Progress, "Literacy: Profiles of America's Young Adults" (1985) sets ten million as the upper limit of the number of illiterate Americans. The Coalition for Literacy puts the number at 27 million Americans—about one adult in five. The professional journal of the American Association of Occupational Health Nurses (1986) estimates that 35 million Americans cannot read, and an additional 30-40 million cannot read well enough to understand safety warnings on the job.

Skills of Secondary School Graduates

See, for example, the reports of the National Commission on Excellence in Education (*A Nation at Risk*, April 1983), of the Carnegie Forum on Education and the Economy (*A Nation Prepared*, 1986), and of the National Assessment of Educational Progress (November 1986).

No Coherent Training Policy

According to the National Conference of State Legislatures, 14 different training programs have been adopted and abandoned since 1962.

Elaine Malek told the Commission in San Francisco that private sector involvement in publicly supported employment efforts is hindered by legislative provisions prohibiting wage subsidies for private employers and requiring advance commitments to hire trainees.

Engineering Shortage

Data from the National Research Council of the National Academy of Sciences show that foreign students account for 52.9 percent of engineering enrollment. See also National Science Foundation, *Academic Science/Engineering Graduate Enrollment and Support*, Washington, D.C., 1983.

Wassily Leontief

See Leontief, Wassily, and Faye Duchin, *The Future Impact of Automation on Workers*, New York: Oxford University Press, 1986. The number 15 million which appears in the text is a Commission staff estimate based on the analyses presented, but the number itself does not appear in the volume. However, in a telephone conversation with the Commission staff director in October 1986, Faye Duchin agreed that the number is a reasonable estimate of the shortage of skilled workers based on the most likely projections of the rate of business acquisition of new technologies.

New Competitive Environment

The Department of Commerce reports that less than ten percent of the 376,000 manufacturers in the United States export their products.

During their working life, most individuals work for an average of ten different employers, according to economist Robert Hall ("The Importance of Lifetime Jobs in the U.S. Economy," *American Economic Review*, September 1982). A 1983 study for the Department of Commerce found that the median job tenure for men was four years, and for women, 2.5 years.

The number of high school students studying a foreign language in school has declined since the 1960s. Less than one quarter of the student population was enrolled in a foreign language course in 1982. Degrees earned in foreign languages (B.A., M.A., Ph.D.) fell by over 50 percent between 1971 and 1983 (National Center for Education Statistics, U.S. Department of Education, *Statistical Abstract*, 1986).

No Understanding of Entrepreneurship

University of Michigan political scientist John Jackson's research on public perceptions of entrepreneurs was issued

in June 1986, and widely reported in the public and business press. He concluded that although entrepreneurs and small businesses create most of the jobs in the United States, most of his national sample of 1,000 people were not aware of this fact.

Lack of Knowledge of Economics

Periodic surveys by the Joint Council on Economic Education, including its "Test of Economic Literacy" (1986), indicate that most high school students do not understand how the free enterprise system works.

Several reports from the Joint Council also document the lack of public awareness about economic matters.

Educators Equally Uninformed

Data from the Joint Council on Economic Education indicate that only eight percent of American teachers studied economics as undergraduates, and that most adults cite television as their main source of information on the economy. In the July 9, 1986 *Wall Street Journal*, Nobel Laureate James Tobin of Yale cited a report of the Southern Regional Education Board showing that only one quarter of teachers had studied economics, and the Rhode Island Council of Economic Education reports that only six percent of its teachers ever had a course in economics.

Savings

At the Commission's first meeting in September 1985, these figures were cited by Bruce R. Scott. According to the Department of Commerce publication "International Economic Indicators," the savings rates of West Germany, Canada, and France are twice the U.S. rate; Japan's savings rate is over three times the U.S. rate.

Harvard economist Benjamin M. Friedman notes that continued federal deficits in the range of four to six percent of GNP "will absorb more than half of the private sector's normal net savings" ("Saving, Investment, and Government Deficits," in Scott, *U.S. Competitiveness*, 1985).

Cost of Capital

George Hatsopoulos made an issue of the cost of capital at the New York hearing in June. He prepared a paper entitled "The Cost of Capital," documenting capital costs for the President's Commission on Industrial Competitiveness (October 1984).

D. Bruce Merrifield, assistant secretary for productivity, technology, and innovation at the U.S. Commerce Department, asserts that "the cost of capital in the United States is two to three times higher than in Japan and other countries" ("Don't Ration Innovation," *Enterprise*, February 1985).

Use of Capital

Peter Behr reported this situation in a *Washington Post* article, January 12, 1986. The figures are from the Board of Governors, Federal Reserve System.

Edward L. Hennessey, Jr., chairman and CEO of Allied Corporation, attributes the recent merger upsurge to "merger bankers and lawyers who are overrewarded for dreaming up outlandish deals," and to the availability of "junk bonds" requiring neither equity nor collateral.

These developments, he says, threaten "capital projects, R&D and other long-term programs.... (The) raiders' actions weaken U.S. business and undercut our competitiveness in international markets" (Speech, May 1985, Economic Club of Detroit).

Morgan Stanley economist Stephen S. Roach noted in a May 27, 1985 *Business Week* article that "we've reached the point where corporate debt loads are starting to impinge on capital spending programs."

The Narrow Base of Capitalism

The Federal Reserve System reports that in 1983 only seven percent of all families had a brokerage account, 17 percent had an IRA or Keogh account, and 14 percent had money market accounts. Representative Stan Lundine (D-N.Y.) cited the statistics on stock ownership in a 1984 Congressional economic conference, noting that the lack of widespread ownership is a "major concern" (Joint Economic Commitee and the Congressional Clearinghouse on the Future, *The New Economy: Proceedings of a Congressional Economic Conference*, June 1984).

Aging Equipment

Senator Slade Gorton (R-Wash.) cited these statistics in a 1983 Senate hearing (Committee on Science, Technology, and Space, *Hearing on S.1286: The Role of Technology in Promoting Industrial Competitiveness*, Seattle, November 23, 1983).

Data from the Bureau of Economic Analysis, Department of Commerce (unpublished data, October 1986), confirm that manufacturing equipment in America is becoming older: despite increased expenditures on "durable equipment" in the 1980s, the average age of manufacturing equipment increased from 8.4 years in 1980 to 8.9 years in 1985. This average obscures industry differences: the average age of equipment in primary metals industries is now nearly 13 years; in electronics, by contrast, it is 6.8.

Several other trends are clear from the information

available: (1) Business spending on "durable equipment" has increased by over one third since 1982 (Commerce, *Survey of Current Business*, July 1986). (2) Manufacturers are, for the most part, modernizing existing facilities, not expanding capacity (1985 survey of capital spending plans by McGraw-Hill, Inc.). (3) A major portion of the overall increase in expenditures for "durable equipment" has been devoted to acquiring information processing and not manufacturing equipment. Expenditures on information processing and related equipment increased 41 percent between 1982 and 1985 while industrial equipment expenditures increased 18 percent (Commerce, *Survey of Current Business*, July 1986).

Consumer Debt

Total installment consumer credit, excluding mortgages, was $577 billion in August 1986. According to the Federal Reserve, consumer credit outstanding at the end of 1976 stood at $190.7 billion. *The Wall Street Journal* reported on September 10, 1986 that consumer credit at the end of July 1986 was 14.6 percent higher than during the same period in 1985.

Venture Capital

A 1984 study prepared for the Joint Economic Committee (*Venture Capital and Innovation*) concluded that venture capital firms fund only five percent of the proposals submitted to them, and "only the cream of the crop of entrepreneurial investments receive funding from the venture capital community."

According to *The State of Small Business* (1986), organized venture capital firms "are bypassing smaller deals—those under $400,000." Don L. Gevirtz, chairman and CEO of the Foothill Group, Inc., wrote in 1985 that venture capital has become "almost unavailable" for most companies (*Enterprise*, February 1985).

Despite rapid growth in annual venture capital investment (over $2.5 billion in 1985, according to Venture Economics, Inc.), venture capital firms are "typically not interested" in small start-up ventures, says David Ellsbury of Deloitte Haskins & Sells in Boston (*D&B Reports*, May/June 1986). Small companies that do not show promise of immediate high returns and a good chance of either being acquired or going public within a few years stand little chance in the venture capital market.

Long-Term Financing Difficult

According to the President's 1984 *Report on the State of Small Business*, small firms obtain 39 percent of their funds from external sources; by contrast, large firms raise over 57

percent of their funds outside the firm.

The Federal Reserve System Board of Governors reports in *The State of Small Business* (1986) that the percentage of long-term bank loans used for small loans (under $100,000) declined from 19 percent in August 1979 to 12 percent in May 1985. Similar results were reported in a survey of the National Federation of Independent Business, "Small Business and Credit" (July 1984).

In 1983, the National Federation of Independent Business reported on two nearly identical surveys on banks and commercial credit. The study described the terms of small business loans from banks:

- Ninety-nine percent of loans to small business exceed the prime rate, on average by three percentage points.
- Nearly half (47 percent) of small business loans are for 12 months or less with an average maturity of six months; only 13 percent are for 61 months or more.

Collateral is required to secure most of these loans—50 percent of the short-term and 90 percent of the long-term loans have collateral requirements—and many loans involve a combination of personal and business assets as collateral.

Bias Against Small Business Investment

A 1985 study issued by Congressman Daniel E. Lungren (R-Calif.) on behalf of the Joint Economic Committee investigated the "alleged capital gap" facing small business.

On the basis of its survey of Small Business Investment Companies (SBICs), the committee concluded that small business is discriminated against in capital markets:

- Seventy-two percent of Small Business Investment Company managers, 64 percent of independent venture capitalists, and a majority of corporate venture managers agreed that "institutional investors, including banks, have a bias against investing in small business."
- They listed as the major reasons for the bias:
  - —lack of institutional expertise;
  - —excessive avoidance of risk;
  - —high portfolio costs associated with an active effort to help small business;
  - —inadequate secondary markets for small business loans; and
  - —inadequate risk-adjusted returns.

Raising Equity

Equity markets involve substantial, upfront legal and

accounting costs for both public offerings (registered with the SEC and probably advertised) or private offerings (not registered and not permitted general solicitation). Both offerings require a formal offering document.

The SEC has been quite active in trying to minimize the burdens of these procedures on small firms—it holds an annual SEC Small Business Capital Formation Forum, and in 1979 approved a simplified registration form for small public offerings, S-18. In 1982, it adopted Regulation D, a set of three exemptions governing private offerings.

Impact on Minorities

Earl Graves, editor of *Black Enterprise*, provided ample evidence of the problems of minority small business owners at the Commission's New York hearings. Studies from the Brookings Institution, the Small Business Administration, and the National Federation of Independent Business document the importance of community resources and personal savings in starting small firms and the difficulties minority entrepreneurs face as a consequence. For example, the President's 1984 report on small business points out that the "median 1982 family income of blacks and persons of Spanish origin was 58 percent and 69 percent, respectively, of the median income of all races," and observes, "This condition limits the prospects of these families to accumulate savings to finance business undertakings."

Few Exporters

The President's Commission on Industrial Competitiveness reported in January 1985 that "250 firms account for nearly 85 percent of all U.S. exports." The export potential of small firms was stressed in testimony before the Commission by Michael Czinkota of Georgetown University. Statistics from the Department of Commerce on the export activities of American firms (1981) show that 12.8 percent of manufacturing employment is export-related.

Export Decline

Arthur Domike testified before the Commission in Atlanta on export decline. Between 1980 and 1982, U.S. merchandise exports fell from $224.3 billion to $211.2 billion (*Economic Report of the President,* 1986).

Lack of Government Assistance

In December 1984, the President's Task Force on International Private Enterprise listed some of the mechanisms foreign governments use to promote exports:

"Financing of local currency costs for turnkey projects; inflation insurance for large contracts requiring long

construction periods; exchange risk insurance for foreign currency-denominated loans; mixed credits that combine concessional government funds with commercial funds to produce lower than market-based interest rates and more lenient loan terms for exporters; and tied-aid credits that utilize the government's foreign assistance programs to influence procurement decisions in their exporters' favor. . . ."

Thus, increasingly, U.S. exporters find themselves having to compete against the national treasuries of mercantilist nations.

The task force concluded that the absence of U.S. government support of a similar nature "diminishes opportunities for U.S. private companies, especially small- and medium-sized, to participate in the LDC development process" (*The President's Task Force on International Private Enterprise: A Report to the President*, December 1984, p. 91).

Small Business Administration statistics were cited by Arthur Domike, vice president of Developing Systems, Limited, in testimony before the Commission, August 4, 1986. (The testimony was reported in the Bureau of National Affairs publication, *Daily Labor Report*, August 6, 1986.)

Appendix C

Schedule of Commission Events

The proceedings of these meetings, including the written testimony presented to the Commission, will be available through the National Technical Information Service (NTIS), Department of Commerce, after March 1987.

Commission Meetings

September 10-11, 1985
Washington, D.C.

February 10, 1986
San Antonio, Texas

November 7, 1986
Washington, D.C.

November 18-19, 1985
Washington, D.C.

September 15, 1986
Seattle, Washington

Commission Hearings

December 9, 1985 **Gerald R. Ford Library**
Ann Arbor, Michigan

- *Entrepreneurship*
- *Innovation, Technology, and R&D*

March 14, 1986 **Bank of America**
San Francisco, California

- *Education and Training*
- *Legal and Regulatory Environment for Small Business*

June 9, 1986 **Federal Hall National Memorial**
New York, New York

- *The Economic Outlook*
- *Capital Availability for Small Business*

August 4, 1986 **Carter Center of Emory University**
Atlanta, Georgia

- *Small Business and Exports*
- *International Comparisons*

Appendix D

Meeting and Hearing Testimony

First Meeting September 10-11, 1985 Washington, D.C.

Speakers

The Honorable Clarence J. Brown
Deputy Secretary
Department of Commerce
Topic: International Competitiveness

Bruce R. Scott
Professor
Harvard University
Graduate School of Business Administration
Topic: U.S. Competitiveness in the World Economy

The Honorable Don Ritter
U.S. House of Representatives
Topic: Targeting the Process of Innovation

George Gilder
Author
The Spirit of Enterprise
Topic: The Entrepreneurial Spirit

David Birch
Massachusetts Institute of Technology
Topic: Who Creates Jobs?

Second Meeting November 18-19, 1985 Washington, D.C.

Speakers

Michael Novak
Resident Scholar
American Enterprise Institute
Topic: Spirit of Democratic Capitalism

The Honorable John J. LaFalce
U.S. House of Representatives
Topic: Industrial Policy

Panels

Topic: The Small Business Agenda

Sam Hope
President-Elect
Small Business United
Milwaukee, Wisconsin

Thomas Donley
Director, Small Business Center
U.S. Chamber of Commerce
Washington, D.C.

Walter Stults
President
National Association of Small Business Investment Companies
Washington, D.C.

Virginia Littlejohn
Past-President
National Association of Women Business Owners
Washington, D.C.

Jerry Gulan
Executive Vice President
National Small Business Association
Washington, D. C.

Topic: Business Owners Speak

David Stewart
Partner
Miller, Cassidy, Larroca & Lewin
Washington, D.C.

James Lagos
Partner
Lagos & Lagos
Springfield, Ohio

Duane Pearsall
General Partner
Columbine Venture Fund, Inc.
Englewood, Colorado

Robert Haddad
Partner
Price Waterhouse & Company
Boston, Massachusetts

Earl Hess
President
Lancaster Laboratories
Lancaster, Pennsylvania

Third Meeting February 10, 1986 San Antonio, Texas
Hosted by the Business & Technology Center,
Control Data Corporation

Speakers

Jude Valdez
Executive Director
Center for Economic Development
University of Texas at San Antonio
Topic: Small Business Development Centers

Rebecca J. Heflin
Deputy Executive Director for Business Development
Texas Economic Development Commission
Austin, Texas
Topic: Small Business and Economic Development in Texas

Site Visits in San Antonio
Business & Technology Center
Mil-Tronics Corporation

Robert McKinley
Manager
Control Data Business & Technology Center
San Antonio, Texas
and
John D. Black
General Manager, Operations
Control Data Business & Technology Center
Minneapolis, Minnesota
Topic: Incubators and Job Creation

The Honorable Gary Hart
United States Senate
Washington, D.C.

Fourth Meeting September 15, 1986 Seattle, Washington
Hosted by Rainier National Bank

Speakers

John D. Mangels
President
Rainier National Bank
Seattle, Washington

Other Business
Discussion of Commission Report

The Honorable Rodney Chandler
U.S. House of Representatives
Washington, D.C.

Fifth Meeting November 7, 1986 Washington, D.C.

Speaker

The Honorable Parren J. Mitchell
U.S. House of Representatives
Washington, D.C.

Other Business
Discussion of Commission Report

First Hearing December 9, 1985 Ann Arbor, Michigan
Hosted by the Gerald R. Ford Library

Co-Chairs

Commissioner Camille Haney
Partner
Anderson, Benjamin, Read & Haney
Milwaukee, Wisconsin

Commissioner John Rennie
President
Pacer Systems, Inc.
Billerica, Massachusetts

Witnesses

Topic: Innovation, Technology, and Research and Development

Reed B. Harker
President
Michigan Research Corporation
Ann Arbor, Michigan

Robert Bailey
Director
Ohio Technology Transfer Organization
Columbus, Ohio

Patrick A. Thompson
President
Trans-Matic
Holland, Michigan

Lawrence R. Crockett
Institute of Science & Technology
University of Michigan
Ann Arbor, Michigan

John Galles
Executive Director
Small Business Association of Michigan
Detroit, Michigan

Todd Anuskiewicz
Research Director
Michigan Energy Research & Resource Association
Detroit, Michigan

Topic: Entrepreneurship

Rodney Benson
President
Ann Arbor Chamber of Commerce
Ann Arbor, Michigan

Geri Larkin
Director, Office of New Enterprise Services
Governor's Cabinet Council on Jobs & Economic Development
Lansing, Michigan

Mary McCurry
President
National Association of Women Business Owners
Denver, Colorado

Dwight Carlson
President
Perceptron
Farmington Hills, Michigan

William Schweke
Vice President
Corporation for Enterprise Development
Washington, D.C.

Robert E. Powless
President
Mount Senario College
Ladysmith, Wisconsin

Philip Guyeskey
Manager, Small Business Programs
Michigan State Chamber of Commerce
Lansing, Michigan

William Gleeson
Director, Center for the Study of Entrepreneurship
Marquette University
Milwaukee, Wisconsin

Public Witnesses

Arthur Matthews
Donaldson & Donald
Detroit, Michigan

John Jackson
Institute for Social Research
University of Michigan
Ann Arbor, Michigan

Second Hearing March 14, 1986 San Francisco, California
Hosted by the Bank of America

Co-Chairs

Commissioner Shirley Chilton
Secretary of State & Consumer Services
State of California
Sacramento, California

Commissioner Arthur V. Toupin
Vice Chairman of the Board (Retired)
Bank of America
San Francisco, California

Witnesses

Topic: Education and Training

Luis David Corrales
Director
Chavez & Associates Institute
City of Commerce, California

Henry Levin
Institute for Research on Educational Finance & Governance
Stanford University
Stanford, California

Elaine J. Malek
Consultant
Elaine J. Malek Associates
Fond du Lac, Wisconsin

John M. Rankin
Executive Director
Goodwill Industries of the Inland Counties, Inc.
San Bernardino, California

Judy Semas
President
HOPE
San Jose, California

Nevzer Stacey
Office of Educational Research & Improvement
U.S. Department of Education
Washington, D.C.

William Turner
President
Technology Exchange Center
Garden Grove, California

Oscar Wright
Small Business Advocate
State of California
Sacramento, California

Topic: Legal and Regulatory Environment for Small Business

Bruce Bunner
Insurance Commissioner
State of California
San Francisco, California

Stephen Carroll
Deputy Director
Institute for Civil Justice
The Rand Corporation
Santa Monica, California

Walter Clemens
President, Western Division
Johnson & Higgins
San Francisco, California

Jaime Coira
Treasurer
Concord Engineering, Inc.
Richmond, California

Scott Hauge
Small Business Council
Chamber of Commerce
San Francisco, California

Walter Hoadley
Senior Research Fellow
Hoover Institution
Stanford University
Stanford, California

William P. Molmen
Vice President, State Programs
American Insurance Association
San Francisco, California

Richard M. Pennington
Senior Vice President
The Atlantic Companies
New York, New York

Public Witness

Paul Cramer
Realtor
San Francisco, California

Other Events in San Francisco
Breakfast meeting with San Francisco Chamber of Commerce

Third Hearing June 9, 1986 New York, New York
Hosted by Federal Hall National Memorial

Co-Chairs

Commissioner John Brademas
President
New York University
New York, New York

Commissioner Bernard E. Anderson
Wharton Center for Applied Research
Philadelphia, Pennsylvania

Witnesses

Topic: The Economic Outlook

Beatrice A. Fitzpatrick
President
American Woman's Economic Development Corporation
New York, New York

Peter Fousek
Executive Vice President & Director of Research
Federal Reserve Bank of New York
New York, New York

Roger H. Fulton
Director of Research
A. Gary Shilling & Company
New York, New York

Aaron Gurwitz
Vice President
Salomon Brothers
New York, New York

Ronald J. Moss
Commissioner
New York State Department of Commerce
New York, New York

Topic: Capital Availability for Small Business

Mark A. Bloomfield
President
American Council for Capital Formation
Washington, D.C.

Earl Graves
President & Editor
Black Enterprise Magazine
New York, New York

George N. Hatsopoulos
Chairman of the Board & President
Thermo Electron
Waltham, Massachusetts

Sara Loveland
Director
National Development Council
New York, New York

James Vitarello
President
James Vitarello Development Associates
Washington, D.C.

Other Events in New York

Lunch - Hosted by the New York Stock Exchange

Speaker: John Sloan, Jr.
President & Chief Executive Officer
National Federation of Independent Business
Washington, D.C.

Fourth Hearing August 4, 1986 Atlanta, Georgia
Hosted by the Carter Center of Emory University

Co-Chairs

Commissioner Richard Hammer
National Director, International Tax Services
Price Waterhouse & Company
New York, New York

Commissioner Robert Woodward
Partner
King & Spalding
Atlanta, Georgia

Witnesses

Topic: Small Business and Exports

Michael Czinkota
National Center for Export-Import Studies
Georgetown University
Washington, D.C.

Arthur Domike
Vice President
Developing Systems, Limited
Washington, D.C.

Edward J. Greenblat
Vice President
Chase Trade, Inc.
New York, New York

Carol Martel
International Department
Atlanta Chamber of Commerce
Atlanta, Georgia

Topic: International Comparisons

Charles M. Bruce
Partner
Butler & Binion
Washington, D.C.

Richard Gilmore
President
GIC Agricultural Group
Washington, D.C.

Bill Nourse
President
Brookemeade Hardware & Supply
Nashville, Tennessee

Erwin von Allmen
President
W.C. Smith, Inc.
Philadelphia, Pennsylvania

Other Events in Atlanta

Tour of Jimmy Carter Presidential Library

Appendix E

Authors of Commissioned Papers

Copies of these papers can be obtained from the National Technical Information Service (NTIS), Department of Commerce, after March 1987.

Steven Balkin
Department of Economics
Roosevelt University
Chicago, Illinois
Topic: Self-Employment for Low-Income People

Renee Berger and Michael Mitchell
Teamworks, Inc.
Washington, D.C.
Topic: Overseas Models of Small Business Development

Mark A. Bloomfield and Margo Thorning
American Council for Capital Formation
Washington, D.C.
Topic: Strategies for Increasing Investment in Small Business

Michael Czinkota
Center for Export-Import Studies
Georgetown University
Washington, D.C.
Topic: Encouraging U.S. Exports by Small- and Medium-Sized Firms

Robert W. Davenport
National Development Council
New York, New York
Topic: Capital Gap Facing Small Business in America

Arthur Domike
Developing Systems, Ltd.
Washington, D.C.
Topic: Promoting Small Business Exports

Richard Gilmore
GIC Agricultural Group
Washington, D.C.
Topic: Alternative Approaches to Encouraging Small Business

John Jackson
Institute for Social Research
University of Michigan
Ann Arbor, Michigan
Topic: Small Business and Job Generation

Elaine J. Malek
Fond du Lac, Wisconsin
Topic: Job Training: An Approach That Works

Ruder, Finn & Rotman
New York, New York
Topic: Small Business in America: A Survey

James Vitarello
James Vitarello Development Associates
Washington, D.C.
Topic: Capital for Small Business